Internal Revenue
bulletin

Bulletin No. 1998–34
August 24, 1998

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

T.D.8777, page 4.

Final regulations under section 465 of the Code relate to qualified nonrecourse financing.

EMPLOYEE PLANS

Notice 98–44, page 7.

Weighted average interest rate update. This notice sets forth for determining for August 1998 the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for purposes of the full funding limitation of section 412(c)(7) of the Code as amended by the Omnibus Budget Reconciliation Act of 1987 and by the Uruguay Round Agreements Act (GATT).

EXEMPT ORGANIZATIONS

Announcement 98–80, page 32.

A list is given of organizations now classified as private foundations.

REG-246256–96, page 9.

Proposed regulations under section 4958 of the Code relate to the excise taxes on excess benefit transactions.

ADMINISTRATIVE

Rev. Proc. 98–45, page 8.

Low-income housing tax credit. This procedure publishes the amounts of unused housing credit carryovers allocated to qualified states under section 42(h)(3)(D) of the Code for calendar year 1998.

Notice 98–38, page 7.

SRLY notice. The Treasury Department and the Service are considering an approach to simplify Separate Return Limitation Year (SRLY) rules applicable to consolidated groups. Comments are requested about the advisability of adopting this approach. The new approach would base the SRLY limitation on an expectation of the amount of income to be generated using the methodology of section 382 of the Code.

Announcement 98–77, page 30.

Comments are requested on proposed training materials discussing the application of section 119 of the Code to the provision of employee meals in the hospitality industry.

Announcement 98–78, page 30.

The Service announces a settlement initiative allowing hospitality industry taxpayers to resolve issues relating to the provision of employee meals.

Announcement 98–79, page 31.

The public hearing for proposed regulation REG–209682–94, 1998–17 I.R.B. 20, is changed to September 10, 1998.

Finding Lists begin on page 35.

Department of the Treasury
Internal Revenue Service

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenue at the least cost; serve the public by continually improving the quality of our products and services; and perform in a manner warranting the highest degree of public confidence in our integrity, efficiency, and fairness.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

Part IV.—Items of General Interest.
With the exception of the Notice of Proposed Rulemaking and the disbarment and suspension list included in this part, none of these announcements are consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes a cumulative index for the matters published during the preceding months. These monthly indexes are cumulated on a semiannual basis and are published in the first Bulletin of the succeeding semiannual period, respectively.

For sale by the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402.

Part I. Rulings and Decisions Under the Internal Revenue Code of 1986

Section 465–Qualified Nonrecourse Financing

26 CFR 1.465–27: Qualified nonrecourse financing.

T.D. 8777

DEPARTMENT OF THE TREASURY Internal Revenue Service

26 CFR Part 1

Qualified Nonrecourse Financing Under Section 465(b)(6)

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations on certain issues regarding qualified nonrecourse financing under section 465(b)(6). These final regulations affect individuals and C corporations for which the stock ownership requirement of section 542(a)(2) is satisfied. These regulations provide guidance on certain issues relating to section 465(b)(6).

DATES: *Effective date:* These regulations are effective August 4, 1998.

Applicability dates: See Effective Dates under Supplementary Information of the preamble.

FOR FURTHER INFORMATION CONTACT: Jeff Erickson at (202) 622-3070 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document amends 26 CFR part 1 to provide rules regarding qualified nonrecourse financing under section 465(b)(6). Section 465 limits a taxpayer's loss deduction for an activity to the taxpayer's amount at risk in the activity at the close of the taxable year. A taxpayer's amount at risk generally includes the amount of any cash and the adjusted tax basis of any property contributed by the taxpayer to the activity plus any amounts borrowed for use in the activity to the extent the taxpayer is personally liable for repayment. For the activity of holding real property, section 465(b)(6) provides that a taxpayer may include as an amount at risk the taxpayer's share of any qualified nonrecourse financing that is secured by real property used in the activity of holding real property, even though the taxpayer is not personally liable for repayment of the financing.

On August 13, 1997, the IRS published in the **Federal Register** (62 FR 43295 [REG–105160–97, 1997–37 I.R.B. 22]) a notice of proposed rulemaking regarding section 465(b)(6). A number of comments were received on the proposed regulations. The public hearing scheduled for December 10, 1997, was canceled because no one requested to speak. After considering the written comments, the proposed regulations are adopted as revised by this Treasury decision.

Explanation of Provisions

I. *Secured by Real Property*

A. Proposed Rule

Section 465(b)(6)(A) provides that qualified nonrecourse financing must be secured by real property used in the activity of holding real property. The proposed regulations provided that a financing can be a qualified nonrecourse financing if, in addition to the real property used in the activity of holding real property, the financing is secured by other property that is incidental to the activity of holding real property (incidental property).

B. Discussion of Comments

A commentator recommended that the final regulations clarify the term *incidental property.* Another commentator asked that the IRS and Treasury define incidental property as any property with a value of not more than 15 percent of the value of the real property held by the borrowing partnership. A third commentator explained that real estate partnerships often hold assets in addition to real property and incidental property. This commentator was concerned that only financings held by partnerships that own only real estate assets could satisfy the proposed regulations. Under the final regulations, if the total gross fair market value of property that is neither real property used in the activity of holding real property nor incidental property is less than 10 percent of the total gross fair market value of all the property securing the financing, such other property is ignored in determining whether the financing satisfies the secured-by-real-property requirement.

Another commentator asked for a look-through rule for partnerships that own an interest in another partnership to determine the character of the assets securing a qualified nonrecourse financing. The final regulations adopt this suggestion by requiring a borrower (whether or not a partnership) to determine the character of its assets by treating itself as owning directly its proportional share of the assets in any partnership in which it owns (directly or indirectly through a chain of partnerships) an equity interest. If a borrower pledges a partnership interest as security for a financing, the partnership assets attributable to the borrower's proportional share of the partnership's assets will be treated as security for the financing.

Commentators also asked under what circumstances qualified nonrecourse financing will be treated as secured by real property. Because this issue is closely-related to the determination of whether the personal liability of a partnership will be disregarded, those issues are addressed together and are discussed in II. *Personal Liability* of this preamble.

A commentator suggested that the final regulations adopt a rule to allocate a single debt obligation among multiple brother-sister partnerships when the obligation is secured by the assetsof more than one partnership. The IRS and Treasury believe this issue is beyond the scope of these regulations.

II. *Personal Liability*

A. Proposed Rule

Section 465(b)(6)(B)(iii) provides that, except to the extent provided in regulations, no person may be personally liable for repayment of a qualified nonrecourse financing. The proposed regulations provided that the personal liability of a partnership (including a limited liability company that is treated as a partnership) is disregarded in determining whether a financing is a qualified nonrecourse financing if the entity's only assets are real property used in the activity of holding real property or both real property and other property that is incidental to the activity of holding real property, and no other person is liable for the financing.

B. Discussion of Comments

Commentators focused on how the proposed regulations apply to tiered partnership structures—when a partnership (the upper-tier partnership) owns a partnership interest in another partnership (the lower-tier partnership). These commentators questioned whether the personal liability of an upper-tier partnership that holds, directly or indirectly, only real property or incidental property should disqualify a financing under section 465(b)(6). As mentioned in I. *Secured by Real Property* of this preamble, commentators also requested guidance as to the situations in which a nonrecourse financing will be treated as secured by real property.

In order to address these comments, the final regulations adopt a three-part test. Under the final regulations, the personal liability of any partnership will be disregarded and, provided certain other requirements are satisfied, the financing will be treated as qualified nonrecourse financing secured by real property if (i) the only persons personally liable to repay the financing are partnerships; (ii) each partnership with personal liability holds only property that is permitted as security for qualified nonrecourse financing (applying a look-through rule for lower-tier partnerships); and (iii) in exercising its remedies to collect on the financing in a default or default-like situation, the lender may proceed only against property that is permitted as security for qualified nonrecourse financing and that is held by the partnership or partnerships (applying a look-through rule for lower-tier partnerships). Similar principles apply in determining the treatment of financing incurred by an entity that is disregarded for federal tax purposes under §301.7701–3 of the Procedure and Administration Regulations. The final regulations contain three examples illustrating the application of these rules to tiered partnerships and one example addressing a situation that involves a disregarded entity.

III. *Other Issues*

A commentator asked that the final regulations clarify whether an entity is disregarded for purposes of section 465(b)(6) if that entity is disregarded as separate from its owner under §301.7701–3. An entity that is disregarded as an entity separate from its owner under §301.7701–3 is disregarded under section 465(b)(6). Certain rules that apply to financings involving disregarded entities are discussed above.

Commentators also raised several other issues, including the treatment of publicly traded financing, that are beyond the scope of these regulations.

IV. *Effective Dates*

The final regulations are effective for any financing incurred on or after August 4, 1998. In response to comments, however, the final regulations include a provision allowing taxpayers to apply the regulations retroactively for financing incurred before August 4, 1998. If a taxpayer chooses to apply these regulations retroactively to financing incurred before August 4, 1998, the IRS will require the taxpayer to reduce the amounts at risk as a result of the application of the regulations to taxable years ending before August 4, 1998, only to the extent the application increases the losses allowed for such years.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the regulation does not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f), the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these regulations is Jeff Erickson, Office of the Assistant Chief Counsel (Passthroughs and Special Industries), IRS. However, other personnel from the offices of the IRS and Treasury Department participated in their development.

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Adoption of Amendments to the Regulations

Accordingly, 26 CFR Part 1 is amended as follows:

PART 1–INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding an entry in numerical order to read as follows:

Authority: 26 U.S.C. 7805 * * *
§1.465–27 also issued under 26 U.S.C. 465(b)(6)(B)(iii). * * *

Par. 2. Section 1.465–27 is added to read as follows:

§1.465–27 Qualified nonrecourse financing.

(a) *In general*. Notwithstanding any provision of section 465(b) or the regulations under section 465(b), for an activity of holding real property, a taxpayer is considered at risk for the taxpayer's share of any qualified nonrecourse financing which is secured by real property used in such activity.

(b) *Qualified nonrecourse financing secured by real property*—(1) *In general*. For purposes of section 465(b)(6) and this section, the term *qualified nonrecourse financing* means any financing—

(i) Which is borrowed by the taxpayer with respect to the activity of holding real property;

(ii) Which is borrowed by the taxpayer from a qualified person or represents a loan from any federal, state, or local government or instrumentality thereof, or is guaranteed by any federal, state, or local government;

(iii) For which no person is personally liable for repayment, taking into account paragraphs (b)(3), (4), and (5) of this section; and

(iv) Which is not convertible debt.

(2) *Security for qualified nonrecourse financing*—(i) *Types of property*. For a taxpayer to be considered at risk under section 465(b)(6), qualified nonrecourse financing must be secured only by real

property used in the activity of holding real property. For this purpose, however, property that is incidental to the activity of holding real property will be disregarded. In addition, for this purpose, property that is neither real property used in the activity of holding real property nor incidental property will be disregarded if the aggregate gross fair market value of such property is less than 10 percent of the aggregate gross fair market value of all the property securing the financing.

(ii) *Look-through rule for partnerships.* For purposes of paragraph (b)(2)(i) of this section, a borrower shall be treated as owning directly its proportional share of the assets in a partnership in which the borrower owns (directly or indirectly through a chain of partnerships) an equity interest.

(3) *Personal liability; partial liability.* If one or more persons are personally liable for repayment of a portion of a financing, the portion of the financing for which no person is personally liable may qualify as qualified nonrecourse financing.

(4) *Partnership liability.* For purposes of section 465(b)(6) and this paragraph (b), the personal liability of any partnership for repayment of a financing is disregarded and, provided the requirements contained in paragraphs (b)(1)(i), (ii), and (iv) of this section are satisfied, the financing will be treated as qualified nonrecourse financing secured by real property if—

(i) The only persons personally liable to repay the financing are partnerships;

(ii) Each partnership with personal liability holds only property described in paragraph (b)(2)(i) of this section (applying the principles of paragraph (b)(2)(ii) of this section in determining the property held by each partnership); and

(iii) In exercising its remedies to collect on the financing in a default or default-like situation, the lender may proceed only against property that is described in paragraph (b)(2)(i) of this section and that is held by the partnership or partnerships (applying the principles of paragraph (b)(2)(ii) of this section in determining the property held by the partnership or partnerships).

(5) *Disregarded entities.* Principles similar to those described in paragraph (b)(4) of this section shall apply in determining whether a financing of an entity that is disregarded for federal tax purposes under §301.7701–3 of this chapter is treated as qualified nonrecourse financing secured by real property.

(6) *Examples.* The following examples illustrate the rules of this section:

Example 1. Personal liability of a partnership; incidental property. (i) X is a limited liability company that is classified as a partnership for federal tax purposes. X engages only in the activity of holding real property. In addition to real property used in the activity of holding real property, X owns office equipment, a truck, and maintenance equipment that it uses to support the activity of holding real property. X borrows $500 to use in the activity. X is personally liable on the financing, but no member of X and no other person is liable for repayment of the financing under local law. The lender may proceed against all of X's assets if X defaults on the financing.

(ii) Under paragraph (b)(2)(i) of this section, the personal property is disregarded as incidental property used in the activity of holding real property. Under paragraph (b)(4) of this section, the personal liability of X for repayment of the financing is disregarded and, provided the requirements contained in paragraphs (b)(1)(i), (ii), and (iv) of this section are satisfied, the financing will be treated as qualified nonrecourse financing secured by real property.

Example 2. Bifurcation of a financing. The facts are the same as in *Example 1*, except that A, a member of X, is personally liable for repayment of $100 of the financing. If the requirements contained in paragraphs (b)(1)(i), (ii), and (iv) of this section are satisfied, then under paragraph (b)(3) of this section, the portion of the financing for which A is not personally liable for repayment ($400) will be treated as qualified nonrecourse financing secured by real property.

Example 3. Personal liability; tiered partnerships. (i) UTP1 and UTP2, both limited liability companies classified as partnerships, are the only general partners in Y, a limited partnership. Y borrows $500 with respect to the activity of holding real property. The financing is a general obligation of Y. UTP1 and UTP2, therefore, are personally liable to repay the financing. Under section 752, UTP1's share of the financing is $300, and UTP2's share is $200. No person other than Y, UTP1, and UTP2 is personally liable to repay the financing. Y, UTP1, and UTP2 each hold only real property.

(ii) Under paragraph (b)(4) of this section, the personal liability of Y, UTP1, and UTP2 to repay the financing is disregarded and, provided the requirements of paragraphs (b)(1)(i), (ii), and (iv) of this section are satisfied, UTP1's $300 share of the financing and UTP2's $200 share of the financing will be treated as qualified nonrecourse financing secured by real property.

Example 4. Personal liability; tiered partnerships. The facts are the same as in *Example 3,* except that Y's general partners are UTP1 and B, an individual. Because B, an individual, is also personally liable to repay the $500 financing, the entire financing fails to satisfy the requirement in paragraph (b)(1)(iii) of this section. Accordingly, UTP1's $300 share of the financing will not be treated as qualified nonrecourse financing secured by real property.

Example 5. Personal liability; tiered partnerships. The facts are the same as in *Example 3,* except that Y is a limited liability company and UTP1 and UTP2 are not personally liable for the debt. However, UTP1 and UTP2 each pledge property as security for the loan that is other than real property used in the activity of holding real property and other than property that is incidental to the activity of holding real property. The fair market value of the property pledged by UTP1 and UTP2 is greater than 10 percent of the sum of the aggregate gross fair market value of the property held by Y and the aggregate gross fair market value of the property pledged by UTP1 and UTP2. Accordingly, the financing fails to satisfy the requirement in paragraph (b)(1)(iii) of this section by virtue of its failure to satisfy paragraph (b)(4)(iii) of this section. Therefore, the financing is not qualified nonrecourse financing secured by real property.

Example 6. Personal liability; Disregarded entity. (i) X is a single member limited liability company that is disregarded as an entity separate from its owner for federal tax purposes under §301.7701–3 of this chapter. X owns certain real property and property that is incidental to the activity of holding the real property. X does not own any other property. For federal tax purposes, A, the sole member of X, is considered to own all of the property held by X and is engaged in the activity of holding real property through X. X borrows $500 and uses the proceeds to purchase additional real property that is used in the activity of holding real property. X is personally liable to repay the financing, but A is not personally liable for repayment of the financing under local law. The lender may proceed against all of X's assets if X defaults on the financing.

(ii) X is disregarded so that the assets and liabilities of X are treated as the assets and liabilities of A. However, A is not personally liable for the $500 liability. Provided that the requirements contained in paragraphs (b)(1)(i), (ii), and (iv) of this section are satisfied, the financing will be treated as qualified nonrecourse financing secured by real property with respect to A.

(c) *Effective date.* This section is effective for any financing incurred on or after August 4, 1998. Taxpayers, however, may apply this section retroactively for financing incurred before August 4, 1998.

Michael P. Dolan,
Deputy Commissioner of Internal Revenue.

Approved July 16, 1998.

Donald C. Lubick,
Assistant Secretary of the Treasury (Tax Policy).

(Filed by the Office of the Federal Register on August 3, 1998, 8:45 a.m., and published in the issue of the Federal Register for August 4, 1998, 63 F.R. 41420)

Part III. Administrative, Procedural, and Miscellaneous

SRLY Notice

Notice 98–38

In 1991, the Treasury Department and the Internal Revenue Service issued proposed regulations concerning the application of the separate return limitation year (SRLY) rules to net operating loss and capital loss carryovers and carrybacks, and built-in deductions. On June 27, 1996, these regulations, substantially unchanged, were re-proposed and issued as temporary regulations in T.D. 8677, 1996–2 C.B. 119. On January 12, 1998 in T.D. 8751, 1998–10 I.R.B. 23, (modified only as to effective date on March 16, 1998 in T.D. 8766, 1998–16 I.R.B. 17) the Treasury Department and the Service published regulations extending the principles of the new temporary regulations to certain tax credits and related attributes. In addition, T.D. 8751 eliminated the application of the SRLY rules to foreign tax credits and overall foreign losses.

Comments have been received in response to each set of proposed regulations. The preamble to the temporary regulations stated that all of the comments would be considered in finalizing the temporary SRLY regulations. Many of the comments asserted that the amendment to §382 of the Internal Revenue Code in 1986 adequately addressed Congressional concerns regarding loss trafficking. Therefore, some commentators argued, the SRLY rules should be eliminated in whole or in part because the SRLY rules have become superfluous, add unwarranted complexity to the consolidated return system, and are easily avoided. Other commentators have argued that the SRLY rules should be retained.

Treasury and the Service have considered these arguments and believe that limitations on the extent to which a consolidated group can use attributes arising in a separate return limitation year remain necessary to protect the integrity of both the separate return system and the consolidated return system. Treasury and the Service, however, are concerned about any complexity in applying the current SRLY rules, particularly with respect to situations where both the SRLY rules and § 382 apply.

Accordingly, Treasury and the Service are considering, inter alia, an approach that would replace the current SRLY limitation with an approach modeled on § 382. While the temporary regulations base the SRLY limitation on the income actually generated by the SRLY member (or SRLY subgroup), the approach under consideration would base the limitation on an expectation of the amount of income to be generated. In other words, applying the methodology of § 382, the limitation would be determined based on the value of the member's or subgroup's stock at the time it joins the consolidated group, with appropriate adjustments (such as adjustments for recognized built-in gains) to reflect adjustments that would be made under § 382.

Most instances in which a corporation becomes a member of a consolidated group involve an ownership change as defined in § 382(g). In those cases, current law requires taxpayers to calculate two separate loss limitations — the SRLY limitation and the § 382 limitation. By making the SRLY limitation the same as the § 382 limitation, the proposed approach would remove the need to make two sets of calculations, thereby greatly simplifying the loss limitation rules applicable to consolidated groups.

In addition, adoption of this approach would address concerns raised that the SRLY rules are easily avoided through the use of stuffing transactions (e.g., transferring income producing assets to the SRLY member).

Treasury and the Service request comments about the advisability of adopting this approach. In particular, comments are requested with respect to the following:

1. Possible approaches to limit the use of loss carrybacks;
2. The application of this approach to credits (including foreign tax credits) and overall foreign losses arising in separate return limitation years;
3. The interaction of this approach with the operation of § 382(l)(5) (relating to corporations in a Title 11 or similar case);
4. Determination of the effect on an ongoing SRLY subgroup limitation when a member of the subgroup leaves the consolidated group;
5. Whether special valuation rules will be required to apply the § 382 mechanism in situations where there is no § 382 ownership change; and
6. Possible transition rules for corporations that joined a consolidated group before the effective date of any new regulations adopting this proposed approach.

Any regulations adopting a new method of determining the SRLY limitation would be initially issued as a notice of proposed rulemaking. Treasury and the Service would provide taxpayers and their representatives another comment period before regulations adopting such an approach are finalized. The existing temporary regulations will apply at least to taxable years ending on or before December 31, 1998.

Comments should be sent to: CC:DOM:CORP:R (Notice 98–38), room 5228, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. In the alternative, comments may be hand delivered to CC:DOM:CORP:R (Notice 98–38), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC. Alternatively, taxpayers may transmit comments electronically via the IRS Internet site at http://www/irs.ustreas.gov/prod/tax-regs/comments.htm1. To be considered, comments should be received by November 15, 1998.

FOR FURTHER INFORMATION CONTACT: David Kessler or Roy Hirschhorn, of the Office of the Assistant Chief Counsel (Corporate), at (202) 622-7770 (not a toll-free number).

Weighted Average Interest Rate Update

Notice 98–44

Notice 88–73 provides guidelines for determining the weighted average interest rate and the resulting permissible range of interest rates used to calculate current liability for the purpose of the full funding limitation of § 412(c)(7) of the Internal Revenue Code as amended by the Omnibus Budget Reconciliation Act of 1987 and as further amended by the Uruguay Round Agreements Act, Pub. L. 103–465 (GATT).

The average yield on the 30-year Treasury Constant Maturities for July 1998 is 5.68 percent.

The following rates were determined for the plan years beginning in the month shown below.

Month	Year	Weighted Average	90% to 106% Permissible Range	90% to 110% Permissible Range
August	1998	6.51	5.86 to 6.90	5.86 to 7.16

Drafting Information

The principal author of this notice is Donna Prestia of the Employee Plans Division. For further information regarding this notice, call (202) 622-6076 between 2:30 and 3:30 p.m. Eastern time (not a toll-free number). Ms. Prestia's number is (202) 622-7473 (also not a toll-free number).

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26 CFR 601.105: Examination of returns and claims for refund, credit, or abatement; determination of correct tax liability.
(Also Part I, § 42; 1.42–14.)

Rev. Proc. 98–45

SECTION 1. PURPOSE

This revenue procedure publishes the amounts of unused housing credit carryovers allocated to qualified states under § 42(h)(3)(D) of the Internal Revenue Code for calendar year 1998.

SECTION 2. BACKGROUND

Rev. Proc. 92–31, 1992–1 C.B. 775, provides guidance to state housing credit agencies of qualified states on the procedure for requesting an allocation of unused housing credit carryovers under § 42(h)(3)(D). Section 4.06 of Rev. Proc. 92–31 provides that the Internal Revenue Service will publish in the Internal Revenue Bulletin the amount of unused housing credit carryovers allocated to qualified states for a calendar year from a national pool of unused credit authority (the National Pool). This revenue procedure publishes these amounts for calendar year 1998.

SECTION 3. PROCEDURE

The unused housing credit carryover amount allocated from the National Pool by the Secretary to each qualified state for calendar year 1998 is as follows:

Qualified State	*Amount Allocated*
Alabama	$ 22,393
Alaska	3,158
Arizona	23,617
California	167,305
Colorado	20,185
Delaware	3,795
Florida	75,979
Georgia	38,814
Idaho	6,274
Illinois	61,679
Indiana	30,404
Iowa	14,787
Kansas	13,455
Kentucky	20,262
Maine	6,440
Maryland	26,412
Massachusetts	31,721
Michigan	50,677
Minnesota	24,296
Mississippi	14,160
Missouri	28,009
Nebraska	8,591
Nevada	8,695
New Jersey	41,754
New Mexico	8,970
New York	94,038
North Carolina	38,498
North Dakota	3,323
Ohio	57,998
Oklahoma	17,198
Oregon	16,815
Pennsylvania	62,322
Rhode Island	5,117
South Carolina	19,495
South Dakota	3,826
Tennessee	27,832
Texas	100,789
Utah	10,676
Vermont	3,054
Virginia	34,915
Washington	29,087

SECTION 4. EFFECTIVE DATE

This revenue procedure is effective for allocations of housing credit dollar amounts attributable to the National Pool component of a qualified state's housing credit ceiling for calendar year 1998.

DRAFTING INFORMATION

The principal author of this revenue procedure is Christopher J. Wilson of the Office of Assistant Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue procedure, contact Mr. Wilson on (202) 622-3040 (not a toll-free call).

Notice of Proposed Rulemaking

Failure by Certain Charitable Organizations To Meet Certain Qualification Requirements; Taxes on Excess Benefit Transactions

REG–246256–96

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to the excise taxes on excess benefit transactions under section 4958 of the Internal Revenue Code (Code), as well as certain amendments and additions to existing Income Tax Regulations affected by section 4958. Section 4958 was enacted in section 1311 of the Taxpayer Bill of Rights 2. Section 4958 generally is effective for transactions occurring on or after September 14, 1995. Section 4958 imposes excise taxes on transactions that provide excess economic benefits to disqualified persons of public charities and social welfare organizations. The proposed regulations clarify certain definitions and rules contained in section 4958.

DATES: Written comments and requests for a teleconference must be received by November 2, 1998.

ADDRESSES: Send submissions to: CC:DOM:CORP:R (REG–246256–96), room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to: CC:DOM: CORP:T:R (REG–246256–96), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW, Washington, DC. Alternatively, taxpayers may submit comments electronically via the Internet by selecting the "Tax Regs" option on the IRS Home Page, or by submitting comments directly to the IRS Internet site at http://www.irs.us treas.gov/prod/tax _regs/comments.html.

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, Phyllis D. Haney of the Office of Associate Chief Counsel (Employee Benefits and Exempt Organizations), (202) 622-4290; concerning submissions, LaNita VanDyke, (202) 622-7190 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collections of information contained in this notice of proposed rulemaking have been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). Comments on the collections of information should be sent to the **Office of Management and Budget**, Attn: Desk Officer for the Department of Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, OP:FS:FP, Washington, DC 20224. Comments on the collection of information should be received by October 5, 1998. Comments are specifically requested concerning:

Whether the proposed collections of information are necessary for the proper performance of the functions of the **Internal Revenue Service**, including whether the information will have practical utility;

The accuracy of the estimated burden associated with the proposed collections of information (see below);

How the quality, utility, and clarity of the information to be collected may be enhanced;

How the burden of complying with the proposed collections of information may be minimized, including through the application of automated collection techniques or other forms of information technology; and

Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of service to provide information.

The collections of information in this proposed regulation are in 26 CFR §§53.4958–6(a)(2), 53.4958–6(a)(3), 53.4958–6(d)(2), and 53.4958–6(d)(3). This information is required for an applicable tax-exempt organization to avail itself of a rebuttable presumption that payments under a compensation arrangement between the organization and a disqualified person are reasonable, or a transfer of property, right to use property, or any other benefit or privilege between the organization and a disqualified person is at fair market value. This information will be used by the organization's governing body, or committee thereof, to document the basis for its determination that compensation was reasonable or any other benefit was at fair market value. The collections of information are required to obtain the benefit of this rebuttable presumption of reasonableness. The likely recordkeepers are nonprofit institutions.

Estimated total annual recordkeeping burden: 910,083 hours.

The estimated annual burden per recordkeeper varies from 3 hours to 308 hours, depending on individual circumstances, with an estimated weighted average of 6 hours, 3 minutes.

Estimated number of recordkeepers: 150,427

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by the Office of Management and Budget.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Background

This document provides rules regarding section 4958 excise taxes on excess benefit transactions. Section 4958 was added to the Code by the Taxpayer Bill of Rights 2, Public Law 104–168 (110 Stat. 1452), enacted July 30, 1996. The section 4958 excise taxes generally apply to excess benefit transactions occurring on or after September 14, 1995. They do not apply, however, to any benefit arising from a transaction pursuant to any written contract that was binding on September 13, 1995, and continued in force through the time of the transaction.

An excess benefit transaction subject to tax under section 4958 is any transaction in which an economic benefit provided by an applicable tax-exempt organization to, or for the use of, any disqualified person exceeds the value of consideration received by the organization in exchange for the benefit. An excess benefit transaction also includes certain revenue-sharing transactions. An applicable tax-exempt organization is any organization described in section 501(c)(3) (except private foundations) or section 501(c)(4) at the time of the excess benefit transaction or at any time during the five-year period ending on the date of the transaction. The excess benefit is generally the excess of the value of the benefit provided to a disqualified person over the value of the consideration received by the organization.

A disqualified person is any person who was, at any time during the 5-year period ending on the date of the excess benefit transaction, in a position to exercise substantial influence over the affairs of the organization. A disqualified person also includes any family member of a person described in the preceding sentence or any entity in which at least 35 percent of the control or beneficial interest is held by such a person.

There are three taxes under section 4958. Disqualified persons are liable for the first two taxes, which are imposed as follows: Pursuant to section 4958(a)(1), a tax of 25 percent of the excess benefit must be paid by any disqualified person who benefits from an excess benefit transaction with an applicable tax-exempt organization. Pursuant to section 4958(b), a tax of 200 percent of the excess benefit must be paid by any disqualified person who benefits from an excess benefit transaction if that transaction is not corrected before the earlier of either the date a deficiency notice is mailed with respect to the 25 percent tax or the date the 25 percent tax is assessed. Certain organization managers are liable for the third tax, which is imposed as follows: Pursuant to section 4958(a)(2), a tax of 10 percent of the excess benefit must be paid by any organization manager who participates in an excess benefit transaction knowingly, willfully, and without reasonable cause. An organization manager is an officer, director, or trustee of the organization, or any individual having powers or responsibilities similar to those of an officer, director, or trustee. The tax that must be paid by participating organization managers for any one excess benefit transaction cannot exceed $10,000.

The IRS notified the general public of the new section 4958 excise taxes in Notice 96–46 (1996–2 C.B. 112). Notice 96–46 also solicited comments to be used in drafting these proposed regulations.

Comments Received Pursuant to Notice 96–46

In response to its request for comments in Notice 96–46, the IRS received 28 comment letters addressing a variety of topics pertaining to section 4958. Some general comments requested that in applying the section 4958 excise taxes the IRS avoid creating administrative burdens on the vast majority of charities and only scrutinize a narrowly targeted group of charities prone to abuse the inurement prohibition. Most comments, however, focused on specific definitions or other statutory language in section 4958. A brief summary of the most frequently made suggestions follows. All of the comments were given consideration in preparing these proposed regulations.

Commentators made suggestions regarding the definition of disqualified person, including applying a facts and circumstances test that annunciates only general principles; using a test that does not treat all of an organization's officers as necessarily being disqualified persons; deferring to an organization's own internal good-faith identification of disqualified persons; treating certain donors as disqualified persons under standards similar to those for private foundation substantial contributors; clarifying that a donor is not in a position to exercise substantial influence over the affairs of an organization solely by reason of having made a large donation; including as disqualified persons those persons who provide advice and consultation to organizations regarding potential excess benefit transactions; providing that a person does not become a disqualified person with respect to a transaction as a result of the transaction (thus a person who negotiated a compensation arrangement in good faith before entering into an employment relationship would not become a disqualified person by virtue of the negotiation); and excluding certain independent contractors from disqualified person status.

Commentators on the tax to be paid by organization managers who participate in an excess benefit transaction knowingly, willfully, and without reasonable cause suggested the following: defining *organization manager* narrowly; using the principles of the regulations under sections 4946 and 4955 in defining *organization manager;* excluding in-house counsel and independent contractors (attorneys, accountants, etc.) from the definition; using an organization's bylaws as the source of determining whether an individual is an officer, director, or trustee; excluding managers who voted against an excess benefit transaction from joint and several liability for any 10% tax associated with the transaction; using the definitions in current section 4946 private foundation regulations for *knowing, willful,* and *reasonable cause;* allowing managers to rely on advice of legal counsel to prove their participation in a transaction was due to reasonable cause, and expanding the category of persons qualified to render opinions with this effect. Although the proposed regulations provide that only advice of counsel in a reasoned written legal opinion protects organization managers in this regard, the IRS invites further comments on this topic. The IRS also requests that such comments address whether, to be consistent on this point, other regulations (*e.g.*, §53.4941 and §53.4945) should be amended as well.

Numerous comments were received on determining reasonable compensation for services and fair market value in sale or exchange transactions. Commentators asked the IRS to use existing law standards under section 162 for determining reasonable compensation and to provide special standards for new organizations in the start-up phase of operations. With respect to compensation, some commentators also requested objective standards or charts of reasonable compensation amounts; others requested that the regulations not impose strict dollar limitations on what would constitute reasonable compensation.

Several commentators made suggestions regarding the requirement that an organization must demonstrate its intent to treat economic benefits as compensation in order to treat the benefit as being provided in exchange for services. These suggestions included using a facts and circumstances test to determine whether an organization clearly indicated its intent to treat a benefit as compensation; considering certain small amounts inadvertently not included in a disqualified person's reported compensation as *de minimis* and not triggering section 4958 taxes; and allowing a reasonable cause exception under which items that were not reported as compensation could still be treated as provided in exchange for services.

A number of commentators requested that the definition of an excess benefit transaction exclude the provision of certain types of benefits to a disqualified person. These benefits included economic benefits made available to the general public on at least as favorable a basis; economic benefits that are *de minimis* fringe benefits under section 132; reimbursements for expenses of administration of an organization; and incidental benefits.

Commentators provided a wide range of suggestions on the subject of which revenue-sharing arrangements should constitute excess benefit transactions. Suggestions included incorporating existing IRS unpublished guidance in a safe harbor rule; using the principles of Rev. Rul. 69–383 (1969–2 C.B. 113), to determine whether a particular plan of compensation results in prohibited inurement or private benefit; limiting the category of revenue-sharing arrangements that constitute excess benefit transactions to arrangements based on the organization's revenues only; and applying regulations on revenue-sharing arrangements prospectively, with transition rules for existing arrangements.

Many comments were received on the rebuttable presumption of reasonableness that is described in the legislative history as arising when a board of directors approves certain compensation arrangements or other transactions. The following suggestions were submitted in multiple comments: that the presumption apply when an applicable organization's board approves general guidelines for entering into transactions with disqualified persons rather than voting on each individual transaction; that the regulations require a determination of reasonableness at the time the organization makes a payment to a disqualified person; that the presumption apply when approval is given by a compensation committee that is not composed exclusively of directors or trustees; that the board or committee be considered independent if members recuse themselves when they have conflicts of interest; that the regulations clarify whether a joint compensation committee composed of representatives from several affiliated organizations would be a committee of each of the respective boards; that the regulations allow an organization's board to delegate the responsibility for setting compensation to an independent committee; that the regulations use examples to define what is an independent firm that can produce salary surveys that will serve as appropriate data on comparability; that the regulations clarify that the rebuttable presumption is a safe harbor and no negative inference should be drawn if an organization does not avail itself of that safe harbor; and that the regulations clarify that compensation outside the range of comparables is not *per se* unreasonable. Some church representatives submitted comments noting that the religious beliefs of some churches and some state laws regarding churches prevent churches from benefitting from the rebuttable presumption of reasonableness because of the identity of the parties required to approve compensation arrangements or other transactions. While these proposed regulations do not provide a special exception for churches from the requirements that must be met to give rise to the rebuttable presumption, they do provide churches with a special rule stating that the procedures of section 7611 will be used in initiating and conducting any inquiry or examination into whether an excess benefit transaction has occurred between a church and a disqualified person. For purposes of this rule, the reasonable belief required to initiate a church tax inquiry is satisfied if there is a reasonable belief that a section 4958 tax is due from a disqualified person with respect to a transaction involving a church.

Several comments were received on the relationship between revocation of tax-exempt status and the taxes imposed under section 4958, recommending that the regulations follow the legislative history on this question. The IRS intends to exercise its administrative discretion in enforcing the requirements of sections 4958, 501(c)(3) and 501(c)(4) in accordance with the direction given in the legislative history. The legislative history specifically provides that the IRS may still revoke the tax-exempt status of an organization for violating the inurement proscription, with or without imposition of section 4958 excise taxes. It further provides that, in practice, the excise taxes imposed by section 4958 will be the sole sanction imposed in those cases in which the excess benefit does not rise to a level where it calls into question whether, on the whole, the organization functions as a charitable or other tax-exempt organization. In determining whether an excess benefit transaction rises to such a level, factors relating to the organization's general pattern of compliance with the requirements of section 501(c)(3) or (4) and other applicable Federal and State laws will be taken into account. These factors would include whether the organization has been involved in repeated excess benefit transactions; the size and scope of the excess benefit transaction; whether, after concluding that it has been party to an excess benefit transaction, the organization has implemented safeguards to prevent future recurrences; and whether there was compliance with other applicable laws. The IRS intends to publish the factors that it will consider in exercising its administrative discretion in guidance issued in conjunction with the issuance of final regulations under section 4958.

Explanation of Provisions

Overview

This document contains proposed regulations that add new regulations under section 4958, and that amend and add to existing Income Tax and Excise Tax Regulations under sections 4963, 6213, 6501, 7422, and 7611. The explanation of these proposed regulations is grouped into two parts: the substantive section 4958 regulations, and regulations under the provisions amended to reflect various effects of the enactment of section 4958 on abatement, Tax Court petitions, statute of limitations, refund actions, and church tax inquiries and examinations. The proposed §53.4958 regulations are described in more detail in this preamble under Section I, Taxes on excess benefit transactions, immediately below. The proposed amendments and additions to regulations under various procedural and administrative provisions affected by the enactment of section 4958 are described in Section

II, Amendment of regulations under various procedural and administrative provisions, below.

I. Taxes on excess benefit transactions

The proposed regulations describe the three taxes imposed under section 4958 on excess benefit transactions between an applicable tax-exempt organization and a disqualified person. Two of the taxes are paid by certain disqualified persons who benefit economically from a transaction, and the other tax is paid by certain organization managers who participate in the transaction knowingly, willfully, and without reasonable cause.

A disqualified person who receives an excess benefit from a transaction is liable for a tax equal to 25 percent of the excess benefit. If the excess benefit is not corrected within the taxable period, that disqualified person is then liable for a tax of 200 percent of the excess benefit. *Taxable period* is defined as the period beginning on the date the transaction occurs and ending on the earlier of the date of mailing a notice of deficiency for the 25 percent tax or the date on which the 25 percent tax is assessed.

Correction is defined in the proposed regulations as undoing the excess benefit to the extent possible, and taking any additional measures necessary to place the organization in a financial position not worse than that in which it would be if the disqualified person had been dealing under the highest fiduciary standards. Correction of the excess benefit occurs if the disqualified person repays the applicable tax-exempt organization an amount of money equal to the excess benefit, plus any additional amount needed to compensate the organization for the loss of the use of the money or other property during the period commencing on the date the excess benefit transaction occurs and ending on the date the excess benefit is corrected. Correction may also be accomplished, in certain circumstances, by returning property to the organization and taking any additional steps necessary to make the organization whole. If the excess benefit transaction consists of the payment of compensation for services under a contract that has not been completed, termination of the employment or independent contractor relationship between the organization and the disqualified person is not required in order to correct. However, the terms of any ongoing compensation arrangement may need to be modified to avoid future excess benefit transactions. If the excess benefit is corrected within the correction period, then under the rules of section 4961 the 200 percent tax under section 4958(b) is not assessed. If the excess benefit is corrected within the correction period and it is established to the satisfaction of the Secretary that the excess benefit transaction was due to reasonable cause and not to willful neglect, then under the rules of section 4962 the 25 percent tax under section 4958(a)(1) will be abated.

Each organization manager who participated in the excess benefit transaction, knowing that it was such a transaction, unless such participation was not willful and was due to reasonable cause, is liable for a tax equal to 10 percent of the excess benefit, not to exceed an aggregate amount of $10,000 with respect to any one excess benefit transaction. An *organization manager* is, with respect to any applicable tax-exempt organization, any officer, director, or trustee of such organization, or any individual having powers or responsibilities similar to those of officers, directors, or trustees of the organization. Independent contractors, acting in a capacity as attorneys, accountants, and investment managers and advisors, are not officers. Any person who has authority merely to recommend particular administrative or policy decisions, but not to implement them without approval of a superior, is not an officer. An individual who is not an officer, director, or trustee, yet serves on a committee of the governing body of an applicable tax-exempt organization that is invoking the rebuttable presumption of reasonableness (described later in this section) based on the committee's action, however, is an organization manager for purposes of the 10 percent tax.

The definitions provided in the proposed regulations for the terms *participation, knowing, willful,* and *due to reasonable cause* with respect to organization managers for section 4958 purposes parallel the definitions of those terms used with respect to foundation managers in the section 4941 regulations. If an organization manager, after full disclosure of the factual situation to legal counsel (including in-house counsel) relies on the advice of such counsel expressed in a reasoned written legal opinion that a transaction is not an excess benefit transaction under section 4958, that manager's participation in such transaction will ordinarily not be considered *knowing* or *willful*, and will ordinarily be considered *due to reasonable cause,* even if the transaction is subsequently held to be an excess benefit transaction.

With respect to any specific excess benefit transaction, if more than one person is liable for any of the taxes imposed by section 4958, all persons with respect to whom a particular tax is imposed are jointly and severally liable for that tax. For instance, if more than one disqualified person benefits from the same transaction, all the benefitting disqualified persons are jointly and severally liable for the respective section 4958(a)(1) or (b) taxes on that transaction. Where an organization manager also receives an excess benefit from an excess benefit transaction, the manager may be liable for both taxes imposed by section 4958(a).

Except as otherwise provided in the proposed regulations, a transaction occurs on the date on which a disqualified person receives an economic benefit from the applicable tax-exempt organization for federal income tax purposes. In the case of payment of deferred compensation, the transaction occurs on the date the deferred compensation is earned and vested.

The proposed regulations cross-reference sections 6501(e)(3) and 6501(l) and the regulations thereunder, as amended, for statute of limitations rules for section 4958 excise taxes. Thus, the statute of limitations for imposition of tax under section 4958 generally begins to run as of the date the applicable tax-exempt organization files its return (Form 990) for the year in which the excess benefit transaction occurred.

The proposed regulations provide that the taxes imposed on excess benefit transactions apply to transactions occurring on or after September 14, 1995. However, these taxes do not apply to a transaction pursuant to a written contract that was binding on September 13, 1995, and at all times thereafter before the transaction occurred. A written binding contract that is terminable or subject to cancellation by the applicable tax-exempt organization without the disqualified person's consent is treated as a new contract as of the date that any such termination or cancellation, if made, would be effective. If a binding written contract is materially modified (including situations in which the contract is amended to extend its term or to increase the amount of compensation payable to the disqualified person), it is treated as a new contract entered into as of the date of the material modification.

Definition of applicable tax-exempt organization

The proposed regulations generally define an applicable tax-exempt organization as any organization that, without regard to any excess benefit, is or would have been described in sections 501(c)(3) or (4) and exempt from tax under section 501(a) at any time during a five-year period ending on the date of an excess benefit transaction (the lookback period). In the specific case of any transaction occurring before September 14, 2000, the lookback period begins on September 14, 1995, and ends on the date of the transaction.

To be described in section 501(c)(3) for purposes of section 4958, an organization must meet the requirements of section 508 (subject to any applicable exceptions provided by that section). A private foundation as defined in section 509(a) is not an applicable tax-exempt organization for section 4958 purposes. An organization that has applied for and received recognition of exemption as an organization described in section 501(c)(4) is an applicable tax-exempt organization for section 4958 purposes. In addition, an organization that has sought to take advantage of section 501(c)(4) status by filing an application for recognition of exemption under section 501(c)(4) with the IRS, filing an information return as a section 501(c)(4) organization under the Code or regulations promulgated thereunder, or otherwise holding itself out as being described in section 501(c)(4), is an applicable tax-exempt organization for section 4958 purposes.

A foreign organization that receives substantially all of its support from sources outside of the United States is not an applicable tax-exempt organization for section 4958 purposes. Section 4948(b) generally states that chapter 42 taxes, including section 4958 taxes on excess benefit transactions, do not apply to any foreign organization that has received substantially all of its support from sources outside the United States.

Definition of disqualified person

The proposed regulations define a disqualified person as a person who, with respect to any transaction with an applicable tax-exempt organization, at any time during a five-year period beginning after September 13, 1995, and ending on the date of such transaction, was in a position to exercise substantial influence over the affairs of the organization. Certain persons are statutorily defined to be disqualified persons under section 4958(f), including certain family members of disqualified persons (spouse, brothers or sisters (by whole or half blood), spouses of brothers or sisters (by whole or half blood), ancestors, children, grandchildren, great grandchildren, and spouses of children, grandchildren, and great grandchildren), and 35 percent controlled entities (a corporation in which a disqualified person owns more than 35 percent of the combined voting power; a partnership in which a disqualified person owns more than 35 percent of the profits interest; or a trust or estate in which a disqualified person owns more than 35 percent of the beneficial interest).

The proposed regulations specifically identify certain persons as having substantial influence over the affairs of an applicable tax-exempt organization. These specified persons include any individual who serves as a voting member on the governing body of the organization; any individual or individuals who have the power or responsibilities of the president, chief executive officer or chief operating officer of an organization; any individual or individuals who have the power or responsibilities of treasurer or chief financial officer of an organization; and any person who has a material financial interest in certain provider-sponsored organizations in which a hospital that is an applicable tax-exempt organization participates.

The proposed regulations deem two categories of persons not to have substantial influence over the affairs of an applicable tax-exempt organization. The first category comprises other applicable tax-exempt organizations described in section 501(c)(3). The second category comprises any employee who, for the taxable year in which the benefits are provided, receives economic benefits, directly or indirectly from the organization, of less than the amount of compensation referenced for a highly compensated employee in section 414(q)(1)(B)(i), who is not a statutorily-defined disqualified person and not specifically identified by the regulations as having substantial influence, and is not a substantial contributor to the organization within the meaning of section 507(d)(2).

The proposed regulations provide that except as specified in the categories set forth in the statute or the preceding parts of the regulation, the determination of whether a person has substantial influence over the affairs of an organization is based on all relevant facts and circumstances. A person who has managerial control over a discrete segment of an organization may nonetheless be in a position to exercise substantial influence over the affairs of the entire organization. Facts and circumstances tending to show that a person has substantial influence over the affairs of an organization include, but are not limited to, the following: that the person founded the organization; that the person is a substantial contributor (within the meaning of section 507(d)(2)) to the organization; that the person's compensation is based on revenues derived from activities of the organization that the person controls; that the person has authority to control or determine a significant portion of the organization's capital expenditures, operating budget, or compensation for employees; that the person has managerial authority or serves as a key advisor to a person with managerial authority; or that the person owns a controlling interest in a corporation, partnership, or trust that is a disqualified person.

Facts and circumstances tending to show that a person does not have substantial influence over the affairs of an organization include but are not limited to, the following: that the person has taken a *bona fide* vow of poverty as an employee, agent, or on behalf of a religious organization; that the person is an independent contractor, such as an attorney, accountant, or investment manager or advisor, acting in that capacity, unless the person is acting in that capacity with respect to a transaction from which the person might economically benefit either directly or indirectly (aside from fees received for the professional services rendered); and that any preferential treatment a person receives based on the size of that person's donation is also offered to any other donor making a comparable contribution as part of a solicitation intended to attract a substantial number of contributions.

In the case of multiple organizations affiliated by common control or governing documents, the determination of whether a person does or does not have substantial influence will be made separately for each applicable tax-exempt organization.

Excess benefit transaction

The proposed regulations state that an *excess benefit transaction* is any transaction in which an economic benefit is provided by an applicable tax-exempt organization directly or indirectly to, or for the use of, any disqualified person if the value of the economic benefit provided exceeds the value of the consideration (including the performance of services) received for providing such benefit. An excess benefit transaction also includes certain revenue-sharing transactions (described later in this section). A benefit can be provided indirectly if it is provided through one or more entities controlled by or affiliated with the applicable tax-exempt organization.

Certain economic benefits provided by an applicable tax-exempt organization to a disqualified person are disregarded for purposes of section 4958. These include paying reasonable expenses for members of the governing body of an applicable tax-exempt organization to attend meetings of the governing body of the organization, not including expenses for luxury travel or spousal travel; an economic benefit provided to a disqualified person that the disqualified person receives solely as a member of, or volunteer for, the organization, if the benefit is provided to members of the public in exchange for a membership fee of $75 or less per year; and an economic benefit provided to a disqualified person that the disqualified person receives solely as a member of a charitable class the applicable tax-exempt organization intends to benefit.

The proposed regulations provide that the payment of a premium for an insurance policy providing liability insurance to a disqualified person to cover any taxes imposed under this section or indemnification of a disqualified person for such taxes by an applicable tax-exempt organization is not an excess benefit transaction if the premium or the indemnification is treated as compensation to the disqualified person when paid, and the total compensation paid to the disqualified person is reasonable.

The proposed regulations provide that if the amount of the economic benefit provided by the applicable tax-exempt organization exceeds the fair market value of the consideration, the excess is the excess benefit on which tax is imposed by section 4958. Rules concerning the excess benefit in certain revenue-sharing transactions are described later in this section. The fair market value of property is the price at which property or the right to use property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy, sell, or transfer property or the right to use property, and both having reasonable knowledge of relevant facts.

Compensation

Compensation for the performance of services is reasonable only if it is an amount that would ordinarily be paid for like services by like enterprises under like circumstances. Generally, the circumstances to be taken into consideration are those existing at the date when the contract for services was made. However, where reasonableness of compensation cannot be determined based on circumstances existing at the date when the contract for services was made, then that determination is made based on all facts and circumstances, up to and including circumstances as of the date of payment. In no event shall circumstances existing at the date when the contract is questioned be considered in making a determination of the reasonableness of compensation. A written binding contract that is terminable or subject to cancellation by the applicable tax-exempt organization without the disqualified person's consent is treated as a new contract as of the date that any such termination or cancellation, if made, would be effective. If a binding written contract is materially modified (which includes amending the contract to extend its term or increase the amount of compensation payable to the disqualified person), it is treated as a new contract entered into as of the date of the material modification. Examples illustrate whether the reasonableness of compensation can be determined based on circumstances existing at the time a contract for the performance of services was made. In accordance with the legislative history, the fact that a State or local legislative or agency body has authorized or approved a particular compensation package paid to a disqualified person is not determinative of the reasonableness of compensation paid for purposes of section 4958 excise taxes. Under the proposed regulations, the fact that a particular compensation package is authorized or approved by a court also is not determinative of the reasonableness of compensation paid to a disqualified person.

Compensation for purposes of section 4958 includes all items of compensation provided by an applicable tax-exempt organization in exchange for the performance of services by a disqualified person. These items of compensation include, but are not limited to, all forms of cash and noncash compensation, including salary, fees, bonuses, and severance payments paid, and all forms of deferred compensation that is earned and vested, whether or not funded, and whether or not paid under a deferred compensation plan that is a qualified plan under section 401(a). If deferred compensation for services performed in multiple prior years vests in a later year, then that compensation is attributed to the years in which the services were performed. Compensation also includes the amount of premiums paid for liability or any other insurance coverage, as well as any payment or reimbursement by the organization of charges, expenses, fees, or taxes not covered ultimately by the insurance coverage; all other benefits, whether or not included in income for tax purposes, including payments to welfare benefit plans on behalf of the disqualified persons, such as plans providing medical, dental, life insurance, severance pay, and disability benefits, and both taxable and nontaxable fringe benefits (other than working condition fringe benefits described in section 132(d) and *de minimis* fringe benefits described in section 132(e)), including expense allowances or reimbursements or foregone interest on loans that the recipient must report as income on his separate income tax return; and any economic benefit provided by the applicable tax-exempt organization directly or indirectly through another entity, owned, controlled by or affiliated with the applicable tax-exempt organization, whether such other entity is taxable or tax-exempt.

An economic benefit that an applicable tax-exempt organization provides to, or for the use, of a disqualified person is not treated as consideration for the performance of services unless the organization clearly indicates its intent to treat the benefit as compensation when the benefit is paid. An applicable tax-exempt organization will be treated as having intended to provide an economic benefit as compensation for services only if it provides clear and convincing evidence of having that intent when the benefit was paid. An applicable tax-exempt organization can provide clear and convincing evidence of such intent by reporting the economic benefit as compensation on original or amended federal tax information returns with respect to the payment (*e.g.*, Form W–2 or 1099) or with respect to the organization (*e.g.*, Form 990), filed before the commencement of an IRS examination in which the reporting of the benefit is questioned. For purposes of section 4958 and these proposed regulations, an IRS examination of an applicable tax-exempt organization has commenced if the organization has received written notification from the Exempt Organizations Division of an impending Exempt Organizations examination, or written notification of an impending referral for an Exempt Organizations examination, and also includes having been under an Exempt Organizations examination that is now in Appeals or in litigation for issues raised in an Exempt Organizations examination of the period in which the excess benefit transaction occurred. Reporting of an economic benefit to provide clear and convincing evidence of intent is also accomplished if the recipient disqualified person reports the benefit as income on the person's Form 1040 for the year in which the benefit is received. If the amount of an economic benefit paid to a disqualified person is not reported and should have been reported on any information return issued by the applicable tax-exempt organization, and the failure to report was due to reasonable cause as defined under section 6724 regulations, then the organization is deemed to satisfy the clear and convincing evidence requirement. To show that its failure to report an economic benefit that should have been reported on an information return was due to reasonable cause, the applicable tax-exempt organization must establish that there are significant mitigating factors with respect to its failure to report, or the failure arose from events beyond the organization's control, and the organization acted in a responsible manner both before and after the failure occurred. If an organization fails to provide clear and convincing evidence that it intended to provide an economic benefit as compensation for services when paid, any services provided by the disqualified person will not be treated as provided in consideration for the economic benefit.

Transaction in which amount of economic benefit determined in whole or in part by the revenues of one or more activities of the organization

The proposed regulations apply a facts and circumstances test to assess whether a transaction in which the amount of an economic benefit provided by an applicable tax-exempt organization to or for the use of a disqualified person is determined in whole or in part by the revenues of one or more activities of the applicable tax-exempt organization (revenue-sharing transaction) results in inurement, and therefore constitutes an excess benefit transaction. A revenue-sharing transaction may constitute an excess benefit transaction regardless of whether the economic benefit provided to the disqualified person exceeds the fair market value of the consideration provided in return if, at any point, it permits a disqualified person to receive additional compensation without providing proportional benefits that contribute to the organization's accomplishment of its exempt purpose. If the economic benefit is provided as compensation for services, relevant facts and circumstances include, but are not limited to, the relationship between the size of the benefit provided and the quality and quantity of the services provided, as well as the ability of the party receiving the compensation to control the activities generating the revenues on which the compensation is based.

The type of revenue-sharing transaction described in the proposed regulations constitutes an excess benefit transaction if it occurs on or after the date of publication of final regulations. The excess benefit in such a transaction consists of the entire economic benefit provided. Any revenue-sharing transaction occurring after September 13, 1995, may still constitute an excess benefit transaction if the economic benefit provided to the disqualified person exceeds the fair market value of the consideration provided in return. Before the date of publication of final regulations, however, the excess benefit shall consist only of that portion of the economic benefit that exceeds the fair market value of the consideration provided in return. Examples are provided of revenue-sharing transactions that do and do not constitute excess benefit transactions.

Rebuttable presumption that transaction is not an excess benefit transaction

The proposed regulations provide that a compensation arrangement between an applicable tax-exempt organization and a disqualified person is presumed to be reasonable, and a transfer of property, a right to use property, or any other benefit or privilege between an applicable tax-exempt organization and a disqualified person is presumed to be at fair market value, if three conditions are satisfied. The three conditions are as follows: (1) the compensation arrangement or terms of transfer are approved by the organization's governing body or a committee of the governing body composed entirely of individuals who do not have a conflict of interest with respect to the arrangement or transaction; (2) the governing body, or committee thereof, obtained and relied upon appropriate data as to comparability prior to making its determination; and (3) the governing body or committee adequately documented the basis for its determination concurrently with making that determination. The presumption established by satisfying these three requirements may be rebutted by additional information showing that the compensation was not reasonable or that the transfer was not at fair market value.

To the extent permitted under local law, the governing body of an applicable tax-exempt organization may authorize other parties to act on its behalf by following specified procedures that satisfy the three requirements for invoking the rebuttable presumption of reasonableness. An arrangement or transaction that is subsequently approved by the board's designee or designees in accordance with those procedures shall be subject to the rebuttable presumption even though the governing body does not vote separately on the specific arrangement or transaction.

With respect to the first requirement, the proposed regulations provide that the governing body is the board of directors, board of trustees, or equivalent controlling body of the applicable tax-exempt organization. A committee of the governing body may be composed of any individuals permitted under state law to serve on such a committee, and may act on behalf of the governing body to the extent permitted by state law. However, any members of such a committee who are not members of the governing body are deemed to be organization managers for purposes of the tax imposed by section 4958(a)(2) if the organization is invoking the rebuttable presumption based on the actions of the committee. A person is not included on an organization's governing body or committee thereof when the governing body or committee is reviewing a transaction if that person meets with the other members only to answer questions, and otherwise recuses himself from the meeting and is not present during debate and voting on the transaction or compensation arrangement.

The proposed regulations provide that a member of the governing body, or committee thereof, does not have a conflict of interest with respect to a compensation arrangement or transaction if the member is not the disqualified person and is not related to any disqualified person participating in or economically benefitting from the compensation arrangement or transaction; is not in an employment relationship subject to the direction or control of any disqualified person participating in or economically benefitting from the compensation arrangement or transaction; is not receiving compensation or other payments subject to approval by any disqualified person participating in or economically benefitting from the compensation arrangement or transaction; has no material financial interest affected by the compensation arrangement or transaction; and, as prescribed in the legislative history, does not approve a transaction providing economic benefits to any disqualified person participating in the compensation arrangement or transaction, who in turn has approved or will approve a transaction providing economic benefits to the member. An arrangement or transaction has not been approved by a committee of a governing body if, under the governing documents of the organization or state law, the committee's decision must be ratified by the full governing body in order to become effective.

With respect to the second requirement for the rebuttable presumption of reasonableness, the proposed regulations provide that a governing body or committee has appropriate data on comparability if, given the knowledge and expertise of its members, it has information sufficient to determine whether a compensation arrangement will result in the payment of reasonable compensation or a transaction will be for fair market value. Relevant information includes, but is not limited to, compensation levels paid by similarly situated organizations, both taxable and tax-exempt, for functionally comparable positions; the availability of similar services in the geographic area of the applicable tax-exempt organization; independent compensation surveys compiled by independent firms; actual written offers from similar institutions competing for the services of the disqualified person; and independent appraisals of the value of property that the applicable tax-exempt organization intends to purchase from, or sell or provide to the disqualified person.

A special rule is provided for organizations with annual gross receipts of less than $1 million. Under this rule, when the governing body reviews compensation arrangements, it will be considered to have appropriate data as to comparability if it has data on compensation paid by five comparable organizations in the same or similar communities for similar services. No inference is intended with respect to whether circumstances falling outside this safe harbor will meet the requirements with respect to the collection of appropriate data.

For purposes of the third requirement of the rebuttable presumption of reasonableness under the proposed regulations, to be documented adequately, the written or electronic records of the governing body or committee must note the terms of the transaction that was approved and the date it was approved; the members of the governing body or committee who were present during debate on the transaction or arrangement that was approved and those who voted on it; the comparability data obtained and relied upon by the committee and how the data was obtained; and the actions taken with respect to consideration of the transaction by anyone who is otherwise a member of the governing body or committee but who had a conflict of interest with respect to the transaction or arrangement. If the governing body or committee determines that reasonable compensation for a specific arrangement or fair market value in a specific transaction is higher or lower than the range of comparable data obtained, the governing body or committee must record the basis for its determination. For a decision to be documented concurrently, records must be prepared by the next meeting of the governing body or committee occurring after the final action or actions of the governing body or committee are taken. Records must be reviewed and approved by the governing body or committee as reasonable, accurate and complete within a reasonable time period thereafter.

If reasonableness of the compensation cannot be determined based on circumstances existing at the date when a contract for services was made, then the rebuttable presumption cannot arise until circumstances exist so that reasonableness of compensation can be determined, and the three requirements for the presumption subsequently are satisfied .

The fact that a transaction between an applicable tax-exempt organization and a disqualified person is not subject to the presumption described in this section shall not create any inference that the transaction is an excess benefit transaction. Neither shall the fact that a transaction qualifies for the presumption exempt or relieve any person from compliance with any federal or state law imposing any obligation, duty, responsibility, or other standard of conduct with respect to the operation or administration of any applicable tax-exempt organization. The rebuttable presumption applies to all payments made or transactions completed in accordance with a contract provided that the three requirements of the rebuttable presumption were met at the time the contract was agreed upon.

Special rules

The proposed regulations provide that the excise taxes imposed by section 4958 do not affect the substantive statutory standards for tax exemption under sections 501(c)(3) or (4). Organizations are described in those sections only if no part of their net earnings inure to the benefit of any private shareholder or individual.

The proposed regulations provide that the procedures of section 7611 will be used in initiating and conducting any inquiry or examination into whether an excess benefit transaction has occurred between a church and a disqualified person. For purposes of this rule, the reasonable belief required to initiate a church tax inquiry is satisfied if there is a reasonable belief that a section 4958 tax is due from a disqualified person with respect to a transaction involving a church. Any additional procedures that apply when determining whether disqualified persons are liable for taxes as a result of transactions with organizations other than churches will apply when determining whether disqualified persons are liable for taxes as a result of transactions with churches.

II. Amendment of regulations under various procedural and administrative provisions

The proposed regulations amend the section 4963 regulations to include section 4958 taxes in the list of taxes subject to abatement under sections 4961 and 4962; amend the section 6213 regulations to suspend the time period for filing a Tax Court petition for the time allowed by the Commissioner to correct a section 4958 transaction; amend the section 6501 regulations to allow the filing of an information return by an applicable tax-exempt organization to begin the three-year limitation on assessment and collection for section 4958 taxes (or six years if an organization failed to disclose an item); amend the section 7422 regulations to apply existing rules for refund proceedings to section 4958 taxes; and amend section 7611 regulations to cross-reference the rules governing the interaction between section 4958 and section 7611 in these proposed regulations.

Except as otherwise specified in the text of the final regulations, these regulations will be effective upon publication of the final regulations in the **Federal Register**. Taxpayers may rely on these proposed regulations for guidance pending the issuance of final regulations. If, and to the extent, future guidance is more restrictive than the guidance in these proposed regulations, the future guidance will be applied without retroactive effect.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required.

An initial regulatory flexibility analysis has been prepared as required for the collection of information in this notice of proposed rulemaking under 5 U.S.C. 603. The analysis follows:

Initial Regulatory Flexibility Analysis

These proposed regulations clarifying section 4958 of the Code (Taxes on excess benefit transactions) may have an impact on small organizations if those organizations avail themselves of the rebuttable presumption of reasonableness described in the regulations (26 C.F.R. §§ 53.4958–6(a)(2), 53.4958–6(a)(3), 53.4958–6(d)(2), and 53.4958–6(d)(3)). The rebuttable presumption is being considered because the legislative history of section 4958 (H. REP. 104–506 at 56–7, March 28, 1996) stated that parties to a transaction should be entitled to rely on such a rebuttable presumption that a compensation arrangement or a property transaction between certain organizations and disqualified persons of the organizations is reasonable or at fair market value. The legislative history further instructed the Secretary of the Treasury and the IRS to issue guidance in connection with the standard for establishing reasonable compensation or fair market value that incorporates this presumption.

The objective for the rebuttable presumption is to allow organizations that satisfy the three requirements to presume that compensation arrangements and property transactions entered into with disqualified persons pursuant to satisfaction of those requirements are reasonable or at fair market value. In such cases, the section 4958 excise taxes can be imposed only if the IRS develops sufficient contrary evidence to rebut the probative value of the evidence put forth by the parties to the transaction. The legal basis for the proposed rule is Code sections 4958 and 7805.

The proposed rule affects organizations described in sections 501(c)(3) and (4) (applicable tax-exempt organizations). Some applicable tax-exempt organizations may be small organizations, defined in 5 U.S.C. 601(4) as any not-for-profit enterprise which is independently owned and operated and is not dominant in its field.

The proposed recordkeeping burden entails obtaining and relying on appropriate comparability data and documenting the basis of an organization's determination that compensation is reasonable, or a property transfer (or transfer of the right to use property) is at fair market value. These actions are necessary to meet two of the requirements specified in the legislative history for obtaining the rebuttable presumption of reasonableness. The skills necessary for these actions are of the type required for obtaining and considering comparability data, and for documenting the membership and actions of the governing board or relevant committee of the organization. Applicable tax-exempt organizations that are small entities of the class that files Form 990–EZ (*i.e.*, those with gross receipts of less than $100,000 and assets of less than $250,000) are unlikely to undertake fulfilling the requirements of the rebuttable presumption of reasonableness, and therefore will not be affected by the recordkeeping burden. All other classes of applicable tax-exempt organizations that file Form 990, up to organizations with assets of $50 million, are likely to be small organizations that avail themselves of the rebuttable presumption of reasonableness. These classes range from organizations with assets of $100,000 to $50 million. The proposed rule currently contains a less burdensome safe harbor for one of the requirements (obtaining comparability data on compensation) for organizations with annual gross receipts of less than $1 million. The IRS is not aware of any other relevant federal rules which may duplicate, overlap, or conflict with the proposed rule. A less burdensome alternative for small organizations would be to exempt those entities from the requirements for establishing the rebuttable presumption of reasonableness. However, it is not consistent with the statute to allow organizations to rely on this presumption without satisfying some conditions. Satisfaction of the requirements as outlined in the legislative history leads to a benefit, but failure to satisfy them does not necessarily lead to a penalty. A more burdensome alternative would be to *require* all applicable tax- exempt organizations under Code section 4958 to satisfy the three requirements of the rebuttable presumption of reasonableness under all circumstances.

Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on business.

Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) that are submitted timely to the IRS. All comments will be available for public inspection and copying. A teleconference public hearing may be scheduled if requested in writing by a person wishing to testify outside the Washington, DC area who timely submits written comments. A request for a hearing by video conference was made on April 7, 1998, by the Taxation Section of the Los Angeles County Bar Association. If a teleconference public hearing is scheduled, notice of the date, time, place, and remote teleconference sites for the hearing will be published in the **Federal Register**.

In addition to several areas mentioned earlier in this preamble, specific comments are requested with respect to certain issues raised by these proposed regulations. Concerning the relationship between revocation of tax-exempt status and the taxes imposed under section 4958, comments are invited to be considered in preparing guidance outlining the factors the IRS will consider in exercising its administrative discretion in accordance with the legislative history. Comments are also requested with regard to the rule under which an economic benefit provided to, or for the use of, a disqualified person will not be treated as consideration for the performance of services absent the clear indication of the organization's intent to treat the benefit as compensation when the benefit is paid. Specifically, comments are requested on appropriate ways of applying this rule that will not create an unnecessary burden on affected organizations. Additionally, comments are requested with respect to the effect of the proposed regulations on different compensation arrangements, including revenue-based compensation, deferred compensation, and the use of options as compensation.

Drafting Information

The principal author of these regulations is Phyllis D. Haney, Office of Associate Chief Counsel (Employee Benefits and Exempt Organizations). However, other personnel from the IRS and Treasury Department participated in their development.

* * * * *

Proposed Amendments to the Regulations

Accordingly, 26 CFR Parts 53 and 301 are proposed to be amended as follows:

PART 53—FOUNDATION AND SIMILAR EXCISE TAXES

Paragraph 1. The authority citation for part 53 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 2. Sections 53.4958–0 through 53.4958–7 are added to read as follows:

§53.4958–0 Table of contents.

This section lists the captions contained in §§53.4958–1 through 53.4958–7.

(d) Persons deemed not to have substantial influence.

(1) Applicable tax-exempt organizations described in section 501(c)(3).

(2) Employees receiving economic benefits of less than specified amount in a taxable year.

(i) In general.

(ii) Examples.

(e) Facts and circumstances govern in all other cases.

(1) In general.

(2) Facts and circumstances tending to show substantial influence.

(3) Facts and circumstances tending to show no substantial influence.

(f) Examples.

(g) Affiliated organizations.

§53.4958–4 Excess benefit transaction.

(a) Definition of excess benefit transaction.

(1) In general.

(2) Economic benefit provided directly or indirectly.

(3) Certain economic benefits disregarded for purposes of section 4958.

(i) Reimbursements for reasonable expenses of attending meetings of governing body.

(ii) Economic benefits provided to a disqualified person solely as a member of, or volunteer for, the organization.

(iii) Economic benefits provided to a disqualified person solely as a member of a charitable class.

(4) Insurance or indemnification of excise taxes.

(b) Standards for identifying excess benefits.

(1) In general.

(2) Fair market value for transfer of property.

(3) Reasonable compensation.

(i) In general.

(ii) Items included in determining the value of compensation for purposes of section 4958.

(iii) Examples.

(c) Establishing intent to treat economic benefit as consideration for the performance of services.

(1) In general.

(2) Clear and convincing evidence of intent.

(i) In general.

(ii) Reporting of benefit.

(iii) Failure to report due to reasonable cause.

(3) Effect of failing to establish intent.

(4) Examples.

§53.4958–5 Transaction in which amount of economic benefit determined in whole or in part by the revenues of one or more activities of the organization.

(a) In general.

(b) Special rule for allocation or return of net margins or capital to members of certain cooperatives.

(c) Rules effective prospectively.

(d) Examples.

§53.4958–6 Rebuttable presumption that transaction is not an excess benefit transaction.

(a) In general.

(b) Delegation pursuant to procedures.

(c) Rebutting the presumption.

(d) Requirements for invoking rebuttable presumption.

(1) Disinterested governing body or committee.

(i) In general.

(ii) Persons not included on governing body or committee.

(iii) Absence of conflict of interest.

(iv) Rule where ratification of full governing body required.

(2) Appropriate data as to comparability.

(i) In general.

(ii) Special rule for compensation paid by small organizations.

(iii) Additional rules for special rule for small organizations.

(iv) Examples.

(3) Documentation.

(e) No presumption until circumstances exist to determine reasonableness of compensation.

(f) No inference from absence of presumption.

(g) Period of reliance on rebuttable presumption.

§53.4958–7 Special rules.

(a) Substantive requirements for exemption still apply.

(b) Interaction between section 4958 and section 7611 rules for church tax inquiries and examinations.

§53.4958–1 Taxes on excess benefit transactions.

(a) *In general.* Section 4958 imposes excise taxes on each excess benefit transaction (as defined in section 4958(c) and §53.4958–4 and §53.4958–5) between an applicable tax-exempt organization (as defined in section 4958(e) and §53.4958–2) and a disqualified person (as defined in section 4958(f)(1) and §53.4958–3). A disqualified person who receives an excess benefit from an excess benefit transaction is liable for payment of a section 4958(a)(1) excise tax equal to 25 percent of the excess benefit. If an initial tax is imposed by section 4958(a)(1) on an excess benefit transaction and the transaction is not corrected within the taxable period, then any disqualified person who received an excess benefit from the excess benefit transaction on which the initial tax was imposed is liable for an additional tax of 200 percent of the excess benefit. An organization manager (as defined in section 4958(f)(2) and paragraph (d) of this section) who participates in an excess benefit transaction, knowing that it was such a transaction, is liable for payment of a section 4958(a)(2) excise tax equal to 10 percent of the excess benefit, unless the participation was not willful and was due to reasonable cause. If an organization manager also receives an excess benefit from an excess benefit transaction, the manager may be liable for both taxes imposed by section 4958(a).

(b) *Excess benefit defined.* Except as provided in §53.4958–5 with respect to certain revenue-sharing transactions, an excess benefit is the value of the economic benefit provided by an applicable tax-exempt organization directly or indirectly to or for the use of any disqualified person that exceeds the value of the consideration (including the performance of services) received by the organization for providing such benefit.

(c) *Taxes paid by disqualified person*—(1) *Initial tax.* Section 4958(a)(1) imposes a tax equal to 25 percent of the excess benefit on each excess benefit transaction. The section 4958(a)(1) tax shall be paid by any disqualified person who received an excess benefit from that excess benefit transaction. With respect to any excess benefit transaction, if more than one disqualified person is liable for the tax imposed by section 4958(a)(1), all such persons are jointly and severally liable for that tax.

(2) *Additional tax on disqualified person*—(i) *In general*. Section 4958(b) im-

poses a tax equal to 200 percent of the excess benefit in any case in which a section 4958(a)(1) tax is imposed on an excess benefit transaction and the transaction is not corrected (as defined in section 4958(f)(6) and paragraph (c)(2)(ii) of this section) within the taxable period (as defined in section 4958(f)(5) and paragraph (c)(2)(iii) of this section). The tax imposed by section 4958(b) is payable by any disqualified person who received an excess benefit from the excess benefit transaction on which the initial tax was imposed by section 4958(a)(1). With respect to any excess benefit transaction, if more than one disqualified person is liable for the tax imposed by section 4958(b), all such persons are jointly and severally liable for that tax.

(ii) *Correction*. *Correction* means, with respect to any excess benefit transaction, undoing the excess benefit to the extent possible, and taking any additional measures necessary to place the organization in a financial position not worse than that in which it would be if the disqualified person had been dealing under the highest fiduciary standards. Correction of the excess benefit occurs if the disqualified person repays the applicable tax-exempt organization an amount of money equal to the excess benefit, plus any additional amount needed to compensate the organization for the loss of the use of the money or other property during the period commencing on the date of the excess benefit transaction and ending on the date the excess benefit is corrected. Correction may also be accomplished, in certain circumstances, by returning property to the organization and taking any additional steps necessary to make the organization whole. If the excess benefit transaction consists of the payment of compensation for services under a contract that has not been completed, termination of the employment or independent contractor relationship between the organization and the disqualified person is not required in order to correct. However, the terms of any ongoing compensation arrangement may need to be modified to avoid future excess benefit transactions.

(iii) *Taxable period*. *Taxable period* means, with respect to any excess benefit transaction, the period beginning with the date on which the transaction occurs and ending on the earlier of–

(A) The date of mailing a notice of deficiency under section 6212 with respect to the section 4958(a)(1) tax; or

(B) The date on which the tax imposed by section 4958(a)(1) is assessed.

(iv) *Abatement if correction during the correction period*. For rules relating to abatement of taxes on excess benefit transactions that are corrected within the correction period, as defined in section 4963(e), see sections 4961(a), 4962(a), and the regulations thereunder.

(d) *Tax paid by organization managers*—(1) *In general*. In any case in which section 4958(a)(1) imposes a tax, section 4958(a)(2) imposes a tax equal to 10 percent of the excess benefit on the participation of any organization manager who knowingly participated in the excess benefit transaction, unless such participation was not willful and was due to reasonable cause. The tax is to be paid by any organization manager who so participated.

(2) *Organization manager defined*—(i) *In general*. An organization manager is, with respect to any applicable tax-exempt organization, any officer, director, or trustee of such organization, or any individual having powers or responsibilities similar to those of officers, directors, or trustees of the organization, regardless of title. A person shall be considered an officer of an organization if–

(A) That person is specifically so designated under the certificate of incorporation, by-laws, or other constitutive documents of the organization; or

(B) That person regularly exercises general authority to make administrative or policy decisions on behalf of the organization. Independent contractors, acting in a capacity as attorneys, accountants, and investment managers and advisors, are not officers. Any person who has authority merely to recommend particular administrative or policy decisions, but not to implement them without approval of a superior, is not an officer.

(ii) *Special rule for certain committee members*. An individual who is not an officer, director, or trustee, yet serves on a committee of the governing body of an applicable tax-exempt organization that is invoking the rebuttable presumption of reasonableness described in §53.4958–6 based on the committee's actions, is an organization manager for purposes of the tax imposed by section 4958(a)(2).

(3) *Participation*. For purposes of section 4958(a)(2) and this paragraph (d), participation includes silence or inaction on the part of an organization manager where the manager is under a duty to speak or act, as well as any affirmative action by such manager. However, an organization manager will not be considered to have participated in an excess benefit transaction where the manager has opposed such transaction in a manner consistent with the fulfillment of the manager's responsibilities to the applicable tax-exempt organization.

(4) *Knowing*—(i) *In general*. For purposes of section 4958(a)(2) and this paragraph (d), a person participates in a transaction knowing that it is an excess benefit transaction only if the person—

(A) Has actual knowledge of sufficient facts so that, based solely upon such facts, such transaction would be an excess benefit transaction;

(B) Is aware that such an act under these circumstances may violate the provisions of federal tax law governing excess benefit transactions; and

(C) Negligently fails to make reasonable attempts to ascertain whether the transaction is an excess benefit transaction, or the person is in fact aware that it is such a transaction.

(ii) *Special rule*. *Knowing* does not mean having reason to know. However, evidence tending to show that a person has reason to know of a particular fact or particular rule is relevant in determining whether the person had actual knowledge of such a fact or rule. Thus, for example, evidence tending to show that a person has reason to know of sufficient facts so that, based solely upon such facts, a transaction would be an excess benefit transaction is relevant in determining whether the person has actual knowledge of such facts.

(5) *Willful*. For purposes of section 4958(a)(2) and this paragraph (d), participation by an organization manager is willful if it is voluntary, conscious, and intentional. No motive to avoid the restrictions of the law or the incurrence of any tax is necessary to make the participation willful. However, participation by an organization manager is not willful if the manager does not know that the transaction in which the manager is participating is an

excess benefit transaction.

(6) *Due to reasonable cause.* An organization manager's participation is due to reasonable cause if the manager has exercised his responsibility on behalf of the organization with ordinary business care and prudence.

(7) *Advice of counsel.* If a person, after full disclosure of the factual situation to legal counsel (including in-house counsel) relies on the advice of such counsel expressed in a reasoned written legal opinion that a transaction is not an excess benefit transaction, the person's participation in such transaction will ordinarily not be considered knowing or willful and will ordinarily be considered due to reasonable cause within the meaning of section 4958(a)(2), even if such transaction is subsequently held to be an excess benefit transaction. For purposes of satisfying the requirements of section 4958(a)(2), a written legal opinion is reasoned so long as the opinion addresses itself to the facts and applicable law. However, a written legal opinion is not reasoned if it does nothing more than recite the facts and express a conclusion. The absence of advice of counsel with respect to an act shall not, by itself, however, give rise to any inference that a person participated in such act knowingly, willfully, or without reasonable cause.

(8) *Limits on liability for management.* The maximum aggregate amount of tax collectible under section 4958(a)(2) and this paragraph (d) from organization managers with respect to any one excess benefit transaction is $10,000.

(9) *Joint and several liability.* In any case where more than one person is liable for a tax imposed by section 4958(a)(2), all such persons shall be jointly and severally liable for the taxes imposed under section 4958(a)(2) with respect to that excess benefit transaction.

(e) *Date of occurrence.* Except as otherwise provided, an excess benefit transaction occurs on the date on which the disqualified person receives the economic benefit from the applicable tax-exempt organization for federal income tax purposes. In the case of a transaction consisting of payment of deferred compensation, the transaction occurs on the date the deferred compensation is earned and vested.

(f) *Statute of limitations.* See sections 6501(e)(3) and 6501(l) and the regulations thereunder, as amended, for statute of limitations rules as they apply to section 4958 excise taxes.

(g) *Effective date for imposition of taxes*—(1) *In general.* The section 4958 taxes imposed on excess benefit transactions or on participation in excess benefit transactions apply to transactions occurring on or after September 14, 1995.

(2) *Existing binding contracts.* The section 4958 taxes do not apply to any transaction occurring pursuant to a written contract that was binding on September 13, 1995, and at all times thereafter before the transaction occurs. A written binding contract that is terminable or subject to cancellation by the applicable tax-exempt organization without the disqualified person's consent is treated as a new contract as of the date that any such termination or cancellation, if made, would be effective. If a binding written contract is materially modified (a material modification includes amending the contract to extend its term or to increase the amount of compensation payable to the disqualified person), it is treated as a new contract entered into as of the date of the material modification.

§53.4958–2 Definition of applicable tax-exempt organization.

(a) *In general*—(1) An applicable tax-exempt organization is any organization that, without regard to any excess benefit, would be described in section 501(c)(3) or (4) and exempt from tax under section 501(a). An applicable tax-exempt organization also includes any organization that was described in section 501(c)(3) or (4) and was exempt from tax under section 501(a) at any time during a five-year period ending on the date of an excess benefit transaction (the lookback period).

(2) In the case of any transaction occurring before September 14, 2000, the lookback period begins on September 14, 1995, and ends on the date of the transaction.

(b) *Section 501(c)(3) organizations.* To be described in section 501(c)(3) for purposes of section 4958, an organization must meet the requirements of section 508 (subject to any applicable exceptions provided by that section). A foreign organization that receives substantially all of its support from sources outside of the United States is not subject to the requirements of section 508 and is not an organization described in section 501(c)(3) for purposes of section 4958. A private foundation as defined in section 509(a) is not an applicable tax-exempt organization for section 4958 purposes.

(c) *Section 501(c)(4) organizations.* An organization that has applied for and received recognition of exemption as an organization described in section 501(c)(4) is an applicable tax-exempt organization for section 4958 purposes. In addition, an organization that has sought to take advantage of section 501(c)(4) status by filing an application for recognition of exemption under section 501(c)(4) with the Internal Revenue Service, filing an information return as a section 501(c)(4) organization under the Internal Revenue Code or regulations promulgated thereunder, or otherwise holding itself out as being described in section 501(c)(4), is an applicable tax-exempt organization for section 4958 purposes. A foreign organization that receives substantially all of its support from sources outside of the United States is not an applicable tax-exempt organization for section 4958 purposes.

§53.4958–3 Definition of disqualified person.

(a) *In general.* Section 4958(f)(1) defines *disqualified person,* with respect to any transaction, as any person who was in a position to exercise substantial influence over the affairs of the organization at any time during the five-year period ending on the date of the transaction. If the five-year period ending on the date of the transaction would have begun on or before September 13, 1995, then the preceding sentence shall be applied to the period beginning September 14, 1995, and ending on the date of the transaction. Paragraph (b) of this section further describes other persons who are defined to be disqualified persons under the statute, including certain family members of an individual in a position to exercise substantial influence, and certain 35 percent controlled entities. Paragraph (c) of this section describes persons in a position to exercise substantial influence over the affairs of an applicable tax-exempt organization by virtue of their powers and responsibilities or certain interests they hold. Paragraph (d) of this section describes persons deemed not to be in a position to exercise substantial influence. Whether any person not described in paragraph (b), (c) or (d) of this section is a disqualified person with respect to the transaction for purposes of section 4958 is based on all relevant facts and circumstances, as described in paragraph (e) of this section. Examples in paragraphs (d)(2)(ii) and (f) of this section illustrate these categories of persons.

(b) *Statutory categories of disqualified persons*—(1) *Family members.* A person is a disqualified person with respect to any transaction with an applicable tax-exempt organization if the person is a member of the family of another disqualified person described in paragraph (a) of this section with respect to any transaction with the same organization. A person's family includes–

(i) Spouse;

(ii) Brothers or sisters (by whole or half blood);

(iii) Spouses of brothers or sisters (by whole or half blood);

(iv) Ancestors;

(v) Children;

(vi) Grandchildren;

(vii) Great grandchildren; and

(viii) Spouses of children, grandchildren, and great grandchildren.

(2) Thirty-five percent controlled entities—(i) *In general.* A person is a disqualified person with respect to any transaction with an applicable tax-exempt organization if the person is a 35 percent controlled entity. A 35 percent controlled entity is–

(A) A corporation in which persons described in this section (except in this paragraph (b)(2) and paragraph (d) of this section) own more than 35 percent of the combined voting power;

(B) A partnership in which persons described in this section (except in this paragraph (b)(2) and paragraph (d) of this section) own more than 35 percent of the profits interest; or

(C) A trust or estate in which persons described in this section (except in this paragraph (b)(2) and paragraph (d) of this section) own more than 35 percent of the beneficial interest.

(ii) *Combined voting power.* For purposes of this paragraph (b)(2), combined voting power includes voting power represented by holdings of voting stock, direct or indirect, but does not include voting rights held only as a director or trustee.

(iii) *Constructive ownership rules*—(A) *Stockholdings.* For purposes of section 4958(f)(3) and this paragraph (b)(2), indirect stockholdings are taken into account as under section 267(c), except that in applying section 267(c)(4), the family of an individual shall include the members of the family specified in section 4958(f)(4) and paragraph (b)(1) of this section.

(B) *Profits or beneficial interest.* For purposes of section 4958(f)(3) and this paragraph (b)(2), the ownership of profits or beneficial interests shall be determined in accordance with the rules for constructive ownership of stock provided in section 267(c) (other than section 267(c)(3)), except that in applying section 267(c)(4), the family of an individual shall include the members of the family specified in section 4958(f)(4) and paragraph (b)(1) of this section.

(c) *Persons having substantial influence.* A person is in a position to exercise substantial influence over the affairs of an applicable tax-exempt organization if that person has the powers or responsibilities, or holds the type of interests, described in one of the following categories:

(1) *Individuals serving on the governing body who are entitled to vote.* This category includes any individual serving on the governing body of the organization who is entitled to vote on matters over which the governing body has authority.

(2) *Presidents, chief executive officers, or chief operating officers.* This category includes any individual who, individually or with others, serves as the president, chief executive officer, or chief operating officer of the organization. An individual serves as a president, chief executive officer, or chief operating officer, regardless of title, if that individual has or shares ultimate responsibility for implementing the decisions of the governing body or supervising the management, administration, or operation of the applicable organization.

(3) *Treasurers and chief financial officers.* This category includes any individual who, independently or with others, serves as treasurer or chief financial officer of the organization. An individual serves as a treasurer or chief financial officer, regardless of title, if that individual has or shares ultimate responsibility for managing the organization's financial assets and has or shares authority to sign drafts or direct the signing of drafts, or authorize electronic transfer of funds, from organization bank accounts.

(4) *Persons with a material financial interest in a provider-sponsored organization.* Pursuant to section 501(o), this category includes any person with a material financial interest in a provider-sponsored organization (as defined in section 1853(e) of the Social Security Act (42 U.S.C. 1395w–23)) if a hospital that participates in the provider-sponsored organization is an applicable tax-exempt organization.

(d) *Persons deemed not to have substantial influence.* A person is deemed not to be in a position to exercise substantial influence over the affairs of an applicable tax-exempt organization if that person is described in one of the following categories:

(1) *Applicable tax-exempt organizations described in section 501(c)(3).* This category includes any other applicable tax-exempt organization described in section 501(c)(3).

(2) *Employees receiving economic benefits of less than specified amount in a taxable year*—(i) *In general.* This category includes, for the taxable year in which benefits are provided, any employee of the applicable tax-exempt organization who–

(A) Receives economic benefits, directly or indirectly from the organization, of less than the amount of compensation referenced for a highly compensated employee in section 414(q)(1)(B)(i);

(B) Is not described in § 53.4958–3(b) or (c) with respect to the organization; and

(C) Is not a substantial contributor to the organization within the meaning of section 507(d)(2).

(ii) *Examples.* The following examples illustrate the category of persons described in this paragraph (d)(2):

Example 1. N, an artist by profession, works part-time at R, a local museum. In the first taxable year in which R employs N, R pays N a modest salary and provides no additional benefits to N except for free admission to the museum, a benefit R provides to all of its employees and volunteers. The total economic benefits N receives from R during the taxable year are less than the amount of compensation referenced for a highly compensated employee in section 414(q)(1)(B)(i). The part-time job constitutes N's only relationship with R. N is not related to any other disqualified person with respect to R. N is deemed not to be in a position to exercise substantial influence over the affairs of R. Therefore N is not a disqualified person with respect to any transaction involving N and R in that year.

Example 2. The facts are the same as in *Example 1,* except that in addition to the modest salary that R pays N in exchange for N's provision of services to R during the taxable year, R also purchases one of N's paintings for $90,000. The total economic benefits provided by R to N in that year exceed the amount of compensation referenced for highly compensated employees in section 414(q)(1)(B)(i). Consequently, whether N is in a position to exercise substantial influence over the affairs of R for that taxable year depends upon all relevant facts and circumstances.

(e) *Facts and circumstances govern in all other cases*—(1) *In general.* Whether a person who is not described in paragraph (b), (c) or (d) of this section is a disqualified person depends upon all relevant facts and circumstances. A person who has managerial control over a discrete segment of an organization may nonetheless be in a position to exercise substantial influence over the affairs of the entire organization.

(2) *Facts and circumstances tending to show substantial influence.* Facts and circumstances tending to show that a person has substantial influence over the affairs of an organization include, but are not limited to, the following—

(i) The person founded the organization;

(ii) The person is a substantial contributor (within the meaning of section 507(d)(2)) to the organization;

(iii) The person's compensation is based on revenues derived from activities of the organization that the person controls;

(iv) The person has authority to control or determine a significant portion of the organization's capital expenditures, operating budget, or compensation for employees;

(v) The person has managerial authority or serves as a key advisor to a person with managerial authority; or

(vi) The person owns a controlling interest in a corporation, partnership, or trust that is a disqualified person.

(3) *Facts and circumstances tending to show no substantial influence.* Facts and circumstances tending to show that a person does not have substantial influence over the affairs of an organization include, but are not limited to–

(i) The person has taken a bona fide vow of poverty as an employee, agent, or on behalf of a religious organization;

(ii) The person is an independent contractor, such as an attorney, accountant, or investment manager or advisor, acting in that capacity, unless the person is acting in that capacity with respect to a transaction from which the person might economically benefit either directly or indirectly (aside from fees received for the professional services rendered); and

(iii) Any preferential treatment a person receives based on the size of that person's donation is also offered to any other donor making a comparable contribution as part of a solicitation intended to attract a substantial number of contributions.

(f) *Examples.* The following examples illustrate the principles of this section. Finding a person to be a disqualified person in the following examples does not indicate that an excess benefit transaction has occurred, but only that any transaction with the applicable tax-exempt organization that provides benefits to the disqualified person directly or indirectly may be scrutinized to determine whether it is an excess benefit transaction:

Example 1. E is the headmaster of Z, a school that is an applicable tax-exempt organization for purposes of section 4958. E reports to Z's board of trustees and is the principal employee responsible for implementing the board's decisions. E also has ultimate responsibility for supervising Z's day-to-day operations. For example, E can hire faculty members and staff, make changes to the school's curriculum and discipline students without specific board approval. Because E serves as the chief executive officer of Z, E is in a position to exercise substantial influence over the affairs of Z. Therefore E is a disqualified person with respect to any transaction involving Z that provides economic benefits to E directly or indirectly.

Example 2. G is a program officer at community organization C, an applicable tax-exempt organization for purposes of section 4958. G's total compensation for the taxable year, including benefits, is less than the amount of compensation referenced for a highly compensated employee in section 414(q)(1)(B)(i). G is not related to any other disqualified person with respect to C. G does not serve on C's governing body and or as an officer of C. G makes a modest annual contribution to C, but is not a substantial contributor to C (within the meaning of section 507(d)(2)). G is deemed not to be in a position to exercise substantial influence over the affairs of C for this year because G is an employee who receives economic benefits for the year of less than the amount of compensation referenced for a highly compensated employee in section 414(q)(1)(B)(i). Therefore, for this year, G is not a disqualified person with respect to any transaction involving C that provides economic benefits to G directly or indirectly.

Example 3. Y, an applicable tax-exempt organization for purposes of section 4958, enters into a contract with B, a company that manages bingo games. Under the contract, B agrees to provide all of the staff and equipment necessary to carry out a bingo operation one night per week, and to pay Y q percent of the revenue from this activity. B retains the balance of the proceeds. Y provides no goods or services in connection with the bingo operation other than the use of its hall for the bingo game. The annual gross revenue earned from the bingo game represents more than half of Y's total annual revenue. B's status as a disqualified person is determined by all relevant facts and circumstances. B's compensation is based on revenues from an activity B controls. B also has full managerial authority over Y's principal source of income. Under these facts and circumstances, B is in a position to exercise substantial influence over the affairs of Y. Therefore B is a disqualified person with respect to any transaction involving Y that provides economic benefits to B directly or indirectly.

Example 4. The facts are the same as in *Example 3,* with the additional fact that the stock of B is 100 percent owned by P, an individual who is actively involved in managing B. Because P owns a controlling interest (measured by either vote or value) in and actively manages B, the facts and circumstances establish that P is also in a position to exercise substantial influence over the affairs of Y. Therefore P is a disqualified person with respect to any transaction involving Y that provides economic benefits to P directly or indirectly.

Example 5. A, an applicable tax-exempt organization for purposes of section 4958, owns and operates one acute care hospital. B is a for-profit corporation that owns and operates a number of hospitals. A and B form C, a limited liability company. In exchange for proportional ownership interests, A contributes its hospital, and B contributes other financial assets, to C. All of A's assets then consist of its membership interest in C. A continues to be operated for exempt purposes based almost exclusively on the activities it conducts through C. C enters into a management agreement with a management company, M, to provide day-to-day management services to C. M is generally subject to supervision by C's board, but M is given broad discretion to manage C's day-to-day operation. Under these facts and circumstances, M is in a position to exercise substantial influence over the affairs of A because it has day to day control over the hospital operated by C, A's ownership interest in C is its primary asset, and C's activities form the basis for A's continued exemption as an organization described in section 501(c)(3). Therefore, M is a disqualified person with respect to any transaction involving A, including any transaction that A conducts through C, that provides economic benefits to M directly or indirectly.

Example 6. T is a large university and an applicable tax-exempt organization for purposes of section 4958. L is the dean of the College of Law of T, a major source of revenue for T. The College of Law is important to T's reputation for excellent teaching and high quality faculty scholarship. T relies on this reputation to attract students and contributions from alumni and foundations. L plays a key role in faculty hiring and has authority to control or determine a significant portion of T's capital expenditures and operating budget because of L's position in the College of Law. L's compensation is greater than the amount of compensation referenced for a highly compensated employee in section 414(q)(1)(B)(i) in the year benefits are provided. Because of the importance of the College of Law to T and L's managerial control over that segment of T, L is in a position to exercise substantial influence over the affairs of T. Therefore L is a disqualified person with respect to any transaction involving T that provides economic benefits to L directly or indirectly.

Example 7. X is a radiologist employed by U, a large acute-care hospital that is an applicable tax-exempt organization for purposes of section 4958. X has no managerial authority over any part of U or its operations. X gives instructions to staff with respect to the radiology work X conducts, but X does not serve as supervisor to other U employees. X's total compensation package includes nontaxable retirement and welfare benefits and a specified amount of salary. X's compensation is greater than the amount of compensation referenced for a highly compensated employee in section 414(q)(1)(B)(i) in the year benefits are provided. X is not related to any other disqualified person of U. X does not serve on U's governing body or as an officer of U. Although U participates in a provider-sponsored organization (as defined in section 1853(e) of the Social Security Act), X does not have a material financial interest in that organization. Whether X is a disqualified person is determined by all relevant facts and circumstances. X did not found U, and although X makes a modest annual financial contribution to U, the amount of the contribution does not make X a substantial contributor within the meaning of section 507(d)(2). X does not receive compensation based on revenues derived from activities of U that X controls, and has no authority to control or determine a significant portion of U's capital expenditures, operating budget, or compensation for employees. Under these facts and circumstances, X does not have substantial influence over the affairs of U, and therefore X is not a disqualified person with respect to any transaction involving U that provides economic benefits to X directly or indirectly.

Example 8. W is a cardiologist and head of the cardiology department of the same hospital U described in *Example 7*. W does not serve on U's board and does not serve as an officer of U. W does not have a material financial interest in the provider-sponsored organization (as defined in section 1853(e) of the Social Security Act) in which U participates. W is compensated personally with a salary and retirement and welfare benefits fixed by a three-year renewable employment contract with U. W's annual amount of compensation exceeds the amount referenced for a highly compensated employee in section 414(q)(1)(B)(i). Whether W is a disqualified person is determined by all relevant facts and circumstances. W has managerial authority for the cardiology department. The cardiology department is a principal source of patients admitted to U and consequently a major source of revenue for U. W also has authority to allocate the budget for that department, which includes authority to distribute incentive bonuses among cardiologists according to criteria that he has authority to set. The pool for the bonuses is funded by a portion of U's revenues attributable to the cardiology department. Because of the importance of the cardiology department to U and W's managerial control over that segment of U, W is in a position to exercise substantial influence over the affairs of U. Therefore W is a disqualified person with respect to any transaction involving U that provides economic benefits to W directly or indirectly.

Example 9. D is an accountant who periodically provides accounting and tax advisory services as an independent contractor in return for a fee to M, a museum that is an applicable tax-exempt organization for purposes of section 4958. For several years, D has advised M's officers and members of M's governing body with respect to accounting and tax matters. D's firm also prepares tax returns on behalf of M. D has no relationship with M other than as a professional accounting and tax advisor. D is not related to any other disqualified person of M. D's firm has a policy prohibiting employees from providing professional advice with respect to a transaction from which they might economically benefit either directly or indirectly (aside from fees received for the professional services rendered). D abides by the firm's policy in all activities, including the work for M. Whether D is a disqualified person is determined by all relevant facts and circumstances. Because D acts only in D's capacity as an independent contractor providing occasional professional services to M and abides by the firm's conflict of interest policy, under these facts and circumstances, D is not a disqualified person with respect to any transaction with M.

Example 10. F, a repertory theater company that is an applicable tax-exempt organization for purposes of section 4958, holds a fund-raising campaign to pay for the construction of a new theater. J is a regular subscriber to F's productions who has made modest gifts to F in the past. J has no relationship to F other than as a subscriber and contributor. F solicits contributions as part of a broad public campaign intended to attract a large number of donors, including a substantial number of donors making large gifts. In its solicitations for contributions, F promises to invite all contributors giving $z or more to a special opening production and party held at the new theater. These contributors are also given a special number to call in F's office to reserve tickets for performances, make ticket exchanges, and make other special arrangements for their convenience. J makes a contribution of $z to F, which makes J a substantial contributor within the meaning of section 507(d)(2). F provides J with the preferential treatment described in its solicitation. Whether J is a disqualified person is determined by all relevant facts and circumstances. Under these facts and circumstances, any influence that may arise from the size of J's donation is limited by F's commitment to provide similar treatment to any other member of the public making a similar contribution and by the nature of the benefits being offered. Accordingly, the preferential treatment that J receives does not indicate that J is in a position to exercise substantial influence over the affairs of the organization. Therefore, barring a change in J's relationship with F, J is not a disqualified person with respect to any transaction involving F that provides economical benefits to J directly or indirectly.

(g) *Affiliated organizations.* In the case of multiple organizations affiliated by common control or governing documents, the determination of whether a person does or does not have substantial influence shall be made separately for each applicable tax-exempt organization.

§53.4958–4 Excess benefit transaction.

(a) Definition of excess benefit transaction—(1) *In general.* An *excess benefit transaction* means any transaction in which an economic benefit is provided by an applicable tax-exempt organization directly or indirectly, to or for the use of, any disqualified person, and the value of the economic benefit provided exceeds the value of the consideration (including the performance of services) received by the organization for providing such benefit. An excess benefit transaction also includes certain revenue-sharing transactions described in §53.4958–5. An economic benefit shall not be treated as consideration for the performance of services unless the organization providing the benefit clearly indicates its intent to treat the benefit as compensation when the benefit is paid.

(2) *Economic benefit provided directly or indirectly.* An excess benefit transaction occurs when an applicable tax-exempt organization provides an excess benefit directly or indirectly to a disqualified person. A benefit may be provided indirectly through the use of one or more entities controlled by or affiliated with the applicable tax-exempt organization. For example, if an applicable tax-exempt organization causes its taxable subsidiary to pay excessive compensation to, or engage in a transaction at other than fair market value with, a disqualified person of the parent organization, the payment of the compensation or the transfer of property is an excess benefit transaction.

(3) *Certain economic benefits disregarded for purposes of section 4958.* The following economic benefits are disregarded for purposes of section 4958:

(i) *Reimbursements for reasonable expenses of attending meetings of governing body.* Paying reasonable expenses for members of the governing body of an applicable tax-exempt organization to attend meetings of the governing body of the organization will be disregarded for purposes of section 4958. For purposes of the preceding sentence, reasonable expenses do not include luxury travel or spousal travel.

(ii) *Economic benefits provided to a disqualified person solely as a member of, or volunteer for, the organization.* An economic benefit provided to a disqualified person that the disqualified person receives solely as a member of, or volunteer for, the organization is disregarded for purposes of section 4958 if the benefit is provided to members of the public in exchange for a membership fee of $75 or less per year. Thus, for example, if a disqualified person is also a member of the organization and receives membership benefits such as advance ticket purchases and a discount at the organization's gift shop that would normally be provided in exchange for a membership fee of $75 or less per year, then the membership benefit is disregarded for purposes of section 4958.

(iii) *Economic benefits provided to a disqualified person solely as a member of a charitable class.* An economic benefit provided to a disqualified person that the disqualified person receives solely as a member of a charitable class that the applicable tax-exempt organization intends to benefit as part of the accomplishment of the organization's exempt purpose is generally disregarded for purposes of section 4958.

(4) *Insurance or indemnification of excise taxes.* The payment of a premium for an insurance policy providing liability insurance to a disqualified person for the taxes imposed under this section or indemnification of a disqualified person for such taxes by an applicable tax-exempt organization will not constitute an excess benefit transaction for purposes of section 4958 if the premium or the indemnification is treated as compensation to the disqualified person when paid, and the total compensation paid to the disqualified person is reasonable.

(b) *Standards for identifying excess benefits*—(1) *In general.* If an economic benefit provided by the applicable tax-exempt organization to or for the use of any disqualified person exceeds the fair market value of the consideration, the excess is the excess benefit on which tax is imposed by section 4958. See §53.4958–5(c) for rules concerning the excess benefit in certain revenue-sharing transactions.

(2) *Fair market value for transfer of property.* The fair market value of property, including the right to use property, is the price at which property or the right to use property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy, sell or transfer property or the right to use property, and both having reasonable knowledge of relevant facts.

(3) *Reasonable compensation*—(i) *In general.* Compensation paid may not exceed what is reasonable under all the circumstances. Compensation for the performance of services is reasonable if it is only such amount as would ordinarily be paid for like services by like enterprises under like circumstances. Generally, the circumstances to be taken into consideration are those existing at the date when the contract for services was made. However, where reasonableness of compensation cannot be determined based on circumstances existing at the date when the contract for services was made, then that determination is made based on all facts and circumstances, up to and including circumstances as of the date of payment. In no event shall circumstances existing at the date when the contract is questioned be considered in making a determination of the reasonableness of compensation. A written binding contract that is terminable or subject to cancellation by the applicable tax-exempt organization without the disqualified person's consent is treated as a new contract as of the date that any such termination or cancellation, if made, would be effective. If a binding written contract is materially modified, it is treated as a new contract entered into as of the date of the material modification. A material modification includes, but is not limited to, amending the contract to extend its term or to increase the amount of compensation payable to the disqualified person. The fact that a State or local legislative or agency body or court has authorized or approved a particular compensation package paid to a disqualified person is not determinative of the reasonableness of compensation paid for purposes of section 4958 excise taxes.

(ii) *Items included in determining the value of compensation for purposes of section 4958.* Compensation for purposes of section 4958 includes all items of compensation provided by an applicable tax-exempt organization in exchange for the performance of services. These items of compensation include, but are not limited to–

(A) All forms of cash and noncash compensation, including salary, fees, bonuses, and severance payments paid;

(B) All forms of deferred compensation that is earned and vested, whether or not funded, and whether or not paid under a deferred compensation plan that is a qualified plan under section 401(a), but if deferred compensation for services performed in multiple prior years vests in a later year, then that compensation is attributed to the years in which the services were performed;

(C) The amount of premiums paid for liability or any other insurance coverage, as well as any payment or reimbursement by the organization of charges, expenses, fees, or taxes not covered ultimately by the insurance coverage;

(D) All other benefits, whether or not included in income for tax purposes, including payments to welfare benefit plans on behalf of the persons being compensated, such as plans providing medical, dental, life insurance, severance pay, and disability benefits, and both taxable and nontaxable fringe benefits (other than working condition fringe benefits described in section 132(d) and de minimis fringe benefits described in section 132(e)), including expense allowances or reimbursements or foregone interest on loans that the recipient must report as income on his separate income tax return; and

(E) Any economic benefit provided by an applicable tax-exempt organization, whether provided directly or through another entity owned, controlled by or affiliated with the applicable tax-exempt organization, whether such other entity is taxable or tax-exempt.

(iii) *Examples.* The following examples illustrate whether the reasonableness of compensation can be determined based on circumstances existing at the time a contract for the performance of services was made under the rules of this paragraph (b)(3):

Example 1. G is an applicable tax-exempt organization for purposes of section 4958. H is an employee of G and a disqualified person with respect to any transaction involving G that provides economic benefits to H directly or indirectly. H's multi-year employment contract provides for payment of a salary and provision of specific amounts of health and retirement benefits. The contract provides for an annual increase in H's salary equal to the percentage increase, if any, over the preceding year in the Consumer Price Index (CPI). The CPI for a year is determined using an average of the monthly CPI as determined for each month in that calendar year. The health benefits consist of insurance coverage under a plan that is available to all of G's employees.

The retirement benefits are equal to the maximum amount G is permitted to contribute under the rules applicable to qualified retirement plans. Under these facts, the reasonableness of H's compensation can be determined based on the circumstances existing at the time G and H enter into the employment contract.

Example 2. N is an applicable tax-exempt organization for purposes of section 4958. N uses the cash method of accounting and a calendar year as its taxable year. On January 2, N's governing body enters into a one-year employment contract for K, its new executive director, who is a disqualified person with respect to any transaction involving N and K. In addition to providing that K will receive a specified amount of salary, deferred compensation, and other health and retirement benefits from N in return for K's services, the terms of the contract permit N's governing body to declare a bonus to be paid to K at any time during the year covered by the contract. Declaration and payment of any bonus is within the governing body's discretion, with no specified limitations or guidelines. The reasonableness of K's compensation cannot be determined based on the circumstances existing as of the date the contract was made because there were no guidelines in the contract for the bonus that N may potentially pay. Therefore, the determination of whether N's compensation is reasonable must be made based on all circumstances, up to and including circumstances as of the date of payment of any bonus actually paid under the contract. If N pays K a bonus on December 31, the reasonableness of K's compensation must be based on all circumstances from January 2 through December 31.

(c) *Establishing intent to treat economic benefit as consideration for the performance of services*—(1) *In general.* An applicable tax-exempt organization will be treated as having intended to provide an economic benefit as compensation for services only if the organization provides clear and convincing evidence that it intended to so treat the economic benefit when the benefit was paid.

(2) *Clear and convincing evidence of intent*—(i) *In general.* If an applicable tax- exempt organization or a disqualified person reports an economic benefit as described in paragraph (c)(2)(ii) of this section then the organization will have provided clear and convincing evidence that it intended to provide an economic benefit as compensation for services when the benefit was paid. If an applicable tax-exempt organization's failure to report an economic benefit as required under the Internal Revenue Code is due to reasonable cause (within the meaning §301.6724–1 of this chapter and paragraph (c)(2)(iii) of this section), then the organization will be treated as having provided clear and convincing evidence of the requisite intent. An organization may use methods other than those described in paragraphs (c)(2)(ii) and (iii) of this section to provide clear and convincing evidence of its intent.

(ii) *Reporting of benefit.* The organization reports the economic benefit as compensation on original or amended federal tax information returns with respect to the payment (*e.g.*, Form W–2 or 1099) or with respect to the organization (*e.g.*, Form 990), filed before the commencement of an Internal Revenue Service examination in which the reporting of the benefit is questioned. For purposes of section 4958 and this section, an Internal Revenue Service examination of an applicable tax-exempt organization has commenced if the organization has received written notification from the Exempt Organizations Division of an impending Exempt Organizations examination, or written notification of an impending referral for an Exempt Organizations examination, and also includes having been under an Exempt Organizations examination that is now in Appeals or in litigation for issues raised in an Exempt Organizations examination of the period in which the excess benefit transaction occurred. Reporting of an economic benefit to provide clear and convincing evidence of intent is also accomplished if the recipient disqualified person reports the benefit as income on the person's Form 1040 for the year in which the benefit is received.

(iii) *Failure to report due to reasonable cause.* To show that its failure to report an economic benefit that should have been reported on an information return was due to reasonable cause, an applicable tax-exempt organization must establish that there were significant mitigating factors with respect to its failure to report (as described in §301.6724–1(b) of this chapter), or the failure arose from events beyond the organization's control (as described in §301.6724–1(c) of this chapter), and that the organization acted in a responsible manner both before and after the failure occurred (as described in §301.6724–1(d) of this chapter).

(3) *Effect of failing to establish intent.* If an organization fails to provide clear and convincing evidence that it intended to provide an economic benefit as compensation for services when paid, any services provided by the disqualified person will not be treated as provided in consideration for the economic benefit.

(4) *Examples.* The following examples illustrate the rules for an organization to establish its intent to treat an economic benefit as consideration for the performance of services as defined in this paragraph (c):

Example 1. G is an applicable tax-exempt organization for purposes of section 4958. G hires an individual contractor, P, to design a computer program for it, executes a contract for that purpose, and pays P $1,000 in a timely manner pursuant to the contract. Before January 31 of the next year, G reports the full amount paid to P under the contract on a Form 1099 filed with the Internal Revenue Service. G has provided clear and convincing evidence of its intent to provide the $1,000 paid to P as compensation for the services P performed under the contract.

Example 2. The facts are the same as in *Example 1,* except that the services are provided by Corporation V. The contract executed by Corporation V and G and placed in G's files indicates that the payment made to Corporation V is in return for computer programming services provided by employees of Corporation V. G does not issue an information return to Corporation V because Corporation V is not an individual taxpayer. The contract constitutes clear and convincing evidence of G's intent to provide the payment as compensation for Corporation V's services.

Example 3. G is an applicable tax-exempt organization for purposes of section 4958. D is the chief operating officer of G, and a disqualified person with respect to any transaction involving G that provides economic benefits to D directly or indirectly. D receives a bonus at the end of the year. A copy of the letter from G to D describing the amount and the basis for D's bonus is placed in D's personnel file. Information provided to all employees in the personnel handbook clearly states that bonuses are treated as taxable income, and included in the total wages figure reported on each employee's Form W–2. G's accounting department determines that the bonus is to be reported on D's Form W–2. Due to a computer malfunction after data was entered incorrectly by personnel of G's accounting department, the bonus is not reflected on D's Form W–2. As a result, D fails to report the bonus on his individual income tax return. G acts to amend Forms W–2 affected as soon as G becomes aware of the data entry error and consequent computer malfunction. G's failure to report the bonus on an information return issued to D arose from events beyond G's control, and G acted in a responsible manner both before and after the failure occurred. Thus, because G had reasonable cause for failing to report D's bonus, G will be treated as having clear and convincing evidence of its intent to provide the bonus as compensation for services when paid.

§53.4958–5 Transaction in which amount of economic benefit determined in whole or in part by the revenues of one or more activities of the organization.

(a) *In general.* Whether a transaction

in which the amount of an economic benefit provided by an applicable tax-exempt organization to or for the use of a disqualified person is determined in whole or in part by the revenues of one or more activities of the applicable tax-exempt organization (revenue-sharing transaction) results in inurement and therefore constitutes an excess benefit transaction, depends upon all relevant facts and circumstances. A revenue-sharing transaction may constitute an excess benefit transaction regardless of whether the economic benefit provided to the disqualified person exceeds the fair market value of the consideration provided in return if, at any point, it permits a disqualified person to receive additional compensation without providing proportional benefits that contribute to the organization's accomplishment of its exempt purpose. If the economic benefit is provided as compensation for services, relevant facts and circumstances include, but are not limited to, the relationship between the size of the benefit provided and the quality and quantity of the services provided, as well as the ability of the party receiving the compensation to control the activities generating the revenues on which the compensation is based.

(b) *Special rule for allocation or return of net margins or capital to members of certain cooperatives.* The allocation or return of net margins or capital to the members of certain cooperatives in accordance with their incorporating statute and bylaws does not result in inurement of the net earnings to the benefit of any private shareholder or individual, and therefore does not constitute an excess benefit transaction for section 4958 purposes. The preceding sentence applies to cooperatives that were determined by the Secretary of the Treasury or his delegate to be described in section 501(c)(4) and exempt from tax under section 501(a) before July 30, 1996, and have substantially the same incorporating statute and bylaws as existed on July 30, 1996.

(c) *Rules effective prospectively.* The rules in this section apply to any revenue-sharing transaction described in this section that occurs on or after the date of publication of final regulations. The excess benefit shall consist of the entire economic benefit provided in any transaction described in this section. Any revenue-sharing transaction occurring after September 13, 1995, may still constitute an excess benefit transaction if the economic benefit provided to the disqualified person exceeds the fair market value of the consideration provided in return. Before the date of publication of final regulations, however, the excess benefit shall consist only of that portion of the economic benefit that exceeds the fair market value of the consideration provided in return.

(d) *Examples.* The following examples illustrate the principles used in determining whether a revenue-sharing transaction constitutes an excess benefit transaction under the rules of this section:

Example 1. A is the manager of the investment portfolio of M, an applicable tax- exempt organization for purposes of section 4958. A and several other professional investment managers work exclusively for M in an office in M's building. A's compensation consists of a flat base annual salary, health insurance, eligibility to participate in a retirement plan, and a bonus that is equal to a percentage of any increase in the value of M's portfolio over the year (net of expenses for investment management other than the in-house managers' compensation). The revenue-based portion of A's compensation gives A an incentive to provide the highest quality service in order to maximize benefits and minimize expenses to M. A has a measure of control over the activities generating the revenues on which his bonus is based, but A can increase his own compensation only if M also receives a proportional benefit. Under these facts and circumstances, the payment to A of the bonus described above does not constitute an excess benefit transaction under the rules of this section.

Example 2. L, an applicable tax-exempt organization for purposes of section 4958, enters into a contract with H, a company who manages charitable gaming activities for public charities. As a result of the contractual relationship, H becomes a disqualified person with respect to any transaction involving L that provides economic benefits to H directly or indirectly. Under the contract, H agrees to provide all of the staff and equipment necessary to carry out charitable gaming operations on behalf of L, and to pay L z percent of the net profits, which are calculated as the gross revenue less rental for the equipment, wages for the staff, prizes for the winners, and other specified operating expenses. H retains the balance of the proceeds after expenses and after paying L its z percent of the net profits. As manager, H controls the activities generating the revenue on which its compensation is based. In addition, because H owns the equipment and employs the staff needed to operate the charitable gaming activities, H controls what L is charged, including the profit H makes above the cost of these items. Therefore, H can also control the net revenues relative to the gross revenues from the gaming activity. The structure of the compensation H receives for its services does not provide H with an appropriate incentive to maximize benefits and minimize costs to L. H benefits whether expenses are high and net revenues are low or expenses are low and net revenues are high. By contrast, L suffers if expenses for the charitable gaming operation are high and net revenues are low. All of the gross revenues generated by the charitable gaming operation belong to L. The arrangement between H and L allows a portion of those revenues to inure to H. Therefore, this arrangement results in the inurement of L's net earnings to the benefit of H, and the entire amount paid to H under this arrangement constitutes an excess benefit under the rules of this section.

Example 3. R, a professor and faculty member at S, a university that is an applicable tax-exempt organization for purposes of section 4958, is the principal investigator in charge of certain scientific research at S. The research produces an invention. In accordance with S's agreement with its faculty, S owns the invention. R assists S in preparing a patent application. S receives a patent for R's invention, which S owns. Also in accordance with S's agreement with its faculty, S grants R the right to receive v percent of S's royalties on the patent, payable semi-annually. R also receives an annual compensation package of salary and benefits. The availability of revenue-based compensation under these circumstances does not give R any incentive or opportunity to act contrary to S's interests in accomplishing its exempt purpose. R receives the revenue-based compensation, i.e., the percentage of royalties, as an incentive and a reward for producing work of especially high quality. In addition, any time R benefits by receiving royalties, S benefits as well and to a proportionate degree. Finally, because the patent belongs to S, R has no control over how the patent is used nor the stream of revenue it generates. Under these facts and circumstances, S's payment of revenue-based compensation to R does not constitute an excess benefit transaction under the rules of this section.

§53.4958–6 Rebuttable presumption that transaction is not an excess benefit transaction.

(a) *In general.* Payments under a compensation arrangement between an applicable tax-exempt organization and a disqualified person shall be presumed to be reasonable, and a transfer of property, right to use property, or any other benefit or privilege between an applicable tax-exempt organization and a disqualified person shall be presumed to be at fair market value, if the following conditions are satisfied–

(1) The compensation arrangement or terms of transfer are approved by the organization's governing body or a committee of the governing body composed entirely of individuals who do not have a conflict of interest with respect to the arrangement or transaction;

(2) The governing body, or committee thereof, obtained and relied upon appropriate data as to comparability prior to

making its determination; and

(3) The governing body or committee adequately documented the basis for its determination concurrently with making that determination.

(b) *Delegation pursuant to procedures.* To the extent permitted under local law, the governing body of an applicable tax-exempt organization may authorize other parties to act on its behalf by following specified procedures that satisfy the three requirements for invoking the rebuttable presumption of reasonableness. An arrangement or transaction that is subsequently approved by the board's designee or designees in accordance with those procedures shall be subject to the rebuttable presumption even though the governing body does not vote separately on the specific arrangement or transaction.

(c) *Rebutting the presumption.* The presumption established by satisfying the three requirements of paragraph (a) of this section may be rebutted by additional information showing that the compensation was not reasonable or that the transfer was not at fair market value.

(d) *Requirements for invoking rebuttable presumption*—(1) *Disinterested governing body or committee*—(i) *In general.* The governing body is the board of directors, board of trustees, or equivalent controlling body of the applicable tax-exempt organization. A committee of the governing body may be composed of any individuals permitted under state law to serve on such a committee, and may act on behalf of the governing body to the extent permitted by state law. However, if the rebuttable presumption arises as the result of actions taken by a committee, any members of such a committee who are not members of the governing body are deemed to be organization managers for purposes of the tax imposed by section 4958(a)(2), subject to the rules of §53.4958–1(d)

(ii) *Persons not included on governing body or committee.* For purposes of determining whether the requirements of paragraph (a) of this section have been met with respect to a specific transaction or compensation arrangement, a person is not included on the governing body or committee when it is reviewing a transaction if that person meets with other members only to answer questions, and otherwise recuses himself from the meeting and is not present during debate and voting on the transaction or compensation arrangement.

(iii) *Absence of conflict of interest.* A member of the governing body, or committee thereof, does not have a conflict of interest with respect to a compensation arrangement or transaction if the member–

(A) Is not the disqualified person and is not related to any disqualified person participating in or economically benefitting from the compensation arrangement or transaction by a relationship described in section 4958(f)(4) or §53.4958–3(b)(1);

(B) Is not in an employment relationship subject to the direction or control of any disqualified person participating in or economically benefitting from the compensation arrangement or transaction;

(C) Is not receiving compensation or other payments subject to approval by any disqualified person participating in or economically benefitting from the compensation arrangement or transaction;

(D) Has no material financial interest affected by the compensation arrangement or transaction; and

(E) Does not approve a transaction providing economic benefits to any disqualified person participating in the compensation arrangement or transaction, who in turn has approved or will approve a transaction providing economic benefits to the member.

(iv) *Rule where ratification by full governing body required.* An arrangement or transaction has not been approved by a committee of a governing body if, under the governing documents of the organization or state law, the committee's decision must be ratified by the full governing body in order to become effective.

(2) *Appropriate data as to comparability*—(i) *In general.* A governing body or committee has appropriate data as to comparability if, given the knowledge and expertise of its members, it has information sufficient to determine whether, under the standards set forth in § 53.4958–4(b), a compensation arrangement will result in the payment of reasonable compensation or a transaction will be for fair market value. Relevant information would include, but not be limited to, compensation levels paid by similarly situated organizations, both taxable and tax-exempt, for functionally comparable positions; the availability of similar services in the geographic area of the applicable tax-exempt organization; independent compensation surveys compiled by independent firms; actual written offers from similar institutions competing for the services of the disqualified person; and independent appraisals of the value of property that the applicable organization intends to purchase from, or sell or provide to, the disqualified person.

(ii) *Special rule for compensation paid by small organizations.* For organizations with annual gross receipts of less than $1 million reviewing compensation arrangements, the governing body or committee will be considered to have appropriate data as to comparability if it has data on compensation paid by five comparable organizations in the same or similar communities for similar services. No inference is intended with respect to whether circumstances falling outside this safe harbor will meet the requirement with respect to the collection of appropriate data.

(iii) *Additional rules for special rule for small organizations.* For purposes of determining applicability of the special rule for small organizations described in paragraph (d)(2)(ii) of this section, a rolling average based on the three prior taxable years may be used to calculate annual gross receipts of an organization. If any applicable tax-exempt organization is affiliated with another entity by common control or governing documents, the annual gross receipts of all such related organizations must be aggregated to determine applicability of the special rule stated in paragraph (d)(2)(ii) of this section.

(iv) *Examples.* The following examples illustrate the rules for appropriate data as to comparability for purposes of invoking the rebuttable presumption of reasonableness described in this section:

Example 1. Z is a large university that is an applicable tax-exempt organization for purposes of section 4958. Z has had gross receipts of $200 million for the preceding three taxable years. Z is negotiating a new contract with its president because the old contract will expire at the end of the year. In determining the compensation for its president, the executive committee of the Board of Trustees relies on a national survey of compensation for university presidents; this survey does not divide its data by any measure of university size or any other criteria. None of the members of the executive committee has any particular expertise in higher education compensation matters, although many members have significant business experience. Given the lack of specificity in the data collected and the lack of relevant expertise and experience of the executive committee members, the data relied on by the executive committee does not constitute appropriate data as to comparability.

Example 2. X, a tax-exempt hospital that is an applicable tax-exempt organization for purposes of section 4958, has average annual gross receipts of $250 million. Before renewing the contracts of X's chief executive officer and chief financial officer, X's governing board commissioned a customized compensation survey from an independent firm that specializes in consulting on issues related to executive placement and compensation. The survey covered executives with comparable responsibilities at a significant number of hospitals. The survey data are sorted by a number of different variables, including the size of the hospitals and the nature of the services they provide, the level of experience and specific responsibilities of the executives, and the composition of the compensation packages. The board members were provided with the survey results, a detailed written analysis comparing the hospital's executives to those covered by the survey and an opportunity to ask questions of a member of the firm that prepared the survey. The survey, as prepared and presented to X's board, constitutes appropriate data as to comparability.

Example 3. W is a local repertory theater and an applicable tax-exempt organization for purposes of section 4958. W has had annual gross receipts ranging from $400,000 to $800,000 over its past three taxable years. In determining the next year's compensation for W's artistic director, the board relies on data compiled from a telephone survey of six other unrelated repertory theaters of similar size in various communities throughout the same geographic region. A member of the board drafts a brief written summary of the salary information obtained from this informal survey. This information is later included in a written report that also includes information about the membership of the board of directors, and an evaluation of the artistic director's prior salary and performance that is discussed and voted on by the board. The salary information obtained in the telephone survey is appropriate data as to comparability.

(3) *Documentation*—(i) For a decision to be documented adequately, the written or electronic records of the governing body or committee must note–

(A) The terms of the transaction that was approved and the date it was approved;

(B) The members of the governing body or committee who were present during debate on the transaction or arrangement that was approved and those who voted on it;

(C) The comparability data obtained and relied upon by the committee and how the data was obtained; and

(D) The actions taken with respect to consideration of the transaction by anyone who is otherwise a member of the governing body or committee but who had a conflict of interest with respect to the transaction or arrangement.

(ii) If the governing body or committee determines that reasonable compensation for a specific arrangement or fair market value in a specific transaction is higher or lower than the range of comparable data obtained, the governing body or committee must record the basis for its determination. For a decision to be documented concurrently, records must be prepared by the next meeting of the governing body or committee occurring after the final action or actions of the governing body or committee are taken. Records must be reviewed and approved by the governing body or committee as reasonable, accurate and complete within a reasonable time period thereafter.

(e) *No presumption until circumstances exist to determine reasonableness of compensation.* If reasonableness of the compensation cannot be determined based on circumstances existing at the date when a contract for services was made, then the rebuttable presumption of this section cannot arise until circumstances exist so that reasonableness of compensation can be determined, and the three requirements for the presumption under paragraph (d) of this section subsequently are satisfied . See §53.4958–4 (b)(3)(i).

(f) *No inference from absence of presumption.* The fact that a transaction between an applicable tax-exempt organization and a disqualified person is not subject to the presumption described in this section shall not create any inference that the transaction is an excess benefit transaction. Neither shall the fact that a transaction qualifies for the presumption exempt or relieve any person from compliance with any federal or state law imposing any obligation, duty, responsibility, or other standard of conduct with respect to the operation or administration of any applicable tax-exempt organization.

(g) *Period of reliance on rebuttable presumption.* The rebuttable presumption applies to all payments made or transactions completed in accordance with a contract provided that the three requirements of the rebuttable presumption were met at the time the contract was agreed upon.

§53.4958–7 Special rules.

(a) *Substantive requirements for exemption still apply.* The excise taxes imposed by section 4958 do not affect the substantive statutory standards for tax exemption under sections 501(c)(3) or (4). Organizations are described in those sections only if no part of their net earnings inure to the benefit of any private shareholder or individual.

(b) *Interaction between section 4958 and section 7611 rules for church tax inquiries and examinations.* The procedures of section 7611 will be used in initiating and conducting any inquiry or examination into whether an excess benefit transaction has occurred between a church and a disqualified person. For purposes of this rule, the reasonable belief required to initiate a church tax inquiry is satisfied if there is a reasonable belief that a section 4958 tax is due from a disqualified person with respect to a transaction involving a church. See §301.7611–1 Q&A 19 of this chapter.

§53.4963–1 [Amended]

Par. 3. In §53.4963–1, paragraphs (a), (b), and (c) are amended by adding the reference "4958," immediately after the reference "4955," in each place it appears.

PART 301—PROCEDURE AND ADMINISTRATION

Par. 4. The authority citation for part 301 continues to read in part as follows:

*Authority: 26 U.S.C. 7805 * * **

§301.6213–1 [Amended]

Par. 5. Section 301.6213–1, paragraph (e) is amended by adding the reference "4958," immediately after the reference "4955," in the first sentence.

§301.6501(e)–1 [Amended]

Par. 6. Section 301.6501(e)–1 is amended as follows:

1. Paragraph (c)(3)(ii), first and second sentences are amended by removing the language "or trust" and adding "trust, or other organization" in its place.

2. Paragraph (c)(3)(ii), the first sentence is amended by removing the language "and 4953" and adding "4953, and 4958" in its place.

§301.6501(n)–1 [Amended]

Par. 7. Section 301.6501(n)–1 is amended as follows:

1. The paragraph heading for paragraph (a) is amended by removing the language *"or trust"* and adding *"trust, or other organization"* in its place.

2. Paragraph (a)(1), the first sentence is amended by removing the language "or trust" and adding "trust, or other organization" in its place.

3. Paragraph (b), the heading and the first sentence are amended by removing the language "or trust" and adding "trust, or other organization" in its place.

§301.7422–1 [Amended]

Par. 8. In section 301.7422–1, paragraphs (a) introductory text, (c) introductory text and (d) are amended by adding the reference "4958," immediately after the reference "4955,".

§301.7611–1 [Amended]

Par. 9. In §301.7611–1, the Table of Contents is amended by adding "Application to Section 4958........19" immediately after "Effective Date........18".

Par. 10. In §301.7611–1, an undesignated centerheading and Q–19 and A–19 are added to read as follows:

§301.7611–1 Questions and answers relating to church tax inquiries and examinations.

* * * * *

Application to Section 4958

Q–19: When do the church tax inquiry and examination procedures described in section 7611 apply to a determination of whether there was an excess benefit transaction described in section 4958?

A–19: See §53.4958–7(b) of this chapter for rules governing the interaction between section 4958 excise taxes on excess benefit transactions and section 7611 church tax inquiry and examination procedures.

Michael P. Dolan,
Deputy Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on July 30, 1998, 9:26 a.m., and published in the issue of the Federal Register for August 4, 1998, 63 F.R. 41486)

Announcement 98–77

The Internal Revenue Service issued today for comment proposed training materials relating primarily to the application of section 119 of the Internal Revenue Code to meals provided to employees in the hospitality industry. The hospitality industry includes casinos, hotels, resorts, and other similar establishments.

You may request a copy of the training materials from Thomas Burger, Director, Office of Employment Tax Administration and Compliance (OETAC), 1111 Constitution Avenue, N.W., Room 2404, OP:EX:ST:ET, Washington, D.C. 20224, or by calling (202) 622-3650 (not a toll-free call). The training materials are also available through the "Tax Professional's Corner" of the IRS Web site at http://www.irs.ustreas.gov. The IRS also issued a settlement initiative allowing hospitality industry taxpayers to resolve issues relating to the provision of employee meals (see Announcement 98–78).

Comments on the proposed training materials are requested by September 30, 1998. Please submit all comments in writing to Dan Bryant, Senior Analyst, Office of Employment Tax Administration and Compliance (OETAC), 1111 Constitution Avenue, N.W., Room 2008, OP:EX:ST:ET, Washington, D.C. 20224.

The principal author of this announcement is Thomas Burger, Director, Office of Employment Tax Administration and Compliance (OETAC). For further information regarding this announcement contact Dan Bryant at (202) 622-3650 (not a toll-free call).

Announcement 98–78

The Internal Revenue Service announces today a settlement initiative under which hospitality industry taxpayers may resolve certain income and employment tax issues covering periods through December 31, 1998, relating to employee meals provided in an employer-operated, on-premises eating facility. The hospitality industry includes casinos, hotels, resorts, and other similar establishments.

Taxpayers who accept the terms of the settlement initiative will resolve these issues quickly and will eliminate the need for further potentially costly controversies for the periods covered by the settlement initiative.

The IRS has decided to offer the settlement initiative as a result of the recent Tax Court decisions in *Boyd Gaming Corp. v. Commissioner,* 106 T.C. No. 19 (1996), and *Boyd Gaming Corp. v. Commissioner,* 72 T.C.M. (RIA) 2912 (September 30, 1997), appeal pending (9th Cir.). Even though the Tax Court opinions addressed some of the issues related to employee meals, other important issues may remain unresolved and thus create uncertainty for taxpayers. The settlement offer is intended to help taxpayers remove that uncertainty for periods through December 31, 1998. The IRS also issued draft training materials relating to employee meals (see Announcement 98–77).

For some taxpayers, a recent statutory change may also resolve uncertainty that has arisen in the wake of the *Boyd Gaming* decisions. Section 5002 of the Internal Revenue Service Restructuring and Reform Act of 1998, P.L. 105–206, added section 119(b)(4) to the Internal Revenue Code. Section 119(b)(4) provides that all meals furnished on the business premises of an employer to an employer's employees are treated as furnished for the convenience of the employer — and therefore are excludable from the employee's income — if more than half of the employees to whom the meals are furnished on the premises are furnished the meals for the convenience of the employer.

The Service recognizes that new section 119(b)(4) may resolve these issues for some hospitality industry taxpayers; however, industry taxpayers whose issues are not resolved by the amendment to section 119 may wish to take advantage of the settlement initiative.

The settlement initiative resolves the following issues:

(1) for the taxpayer, the deductibility of expenses for employee meals provided in an employer-operated, on-premises eating facility;

(2) for the taxpayer, any employment tax liability relating to the provision of employee meals in an employer-operated, on-premises eating facility; and

(3) for the employee, any income tax or employment tax liability relating to the receipt of employee meals in an employer-operated, on-premises eating facility.

If a taxpayer accepts the offer to resolve these issues through this settlement initiative, the following terms will apply with respect to meals provided on or before December 31, 1998:

I. For taxable years beginning before January 1, 1995, the limitation set forth in I.R.C. section 274(n)(1), as in effect for each year at issue, shall apply, without exception, to the expense of providing meals to taxpayer's employees.

II. For taxable years beginning on or after January 1, 1995 and on or before January 1, 1998, the taxpayer may deduct 70% of the otherwise allowable expense (prior to the application of section 274(n)(1)) of providing meals to taxpayer's employees.

III. For taxable years beginning after January 1, 1998 and before December 31, 1998, the taxpayer may deduct 70% of the otherwise allowable expense (prior to the application of section 274(n)(1)) of providing meals to taxpayer's employees for meals provided during the months in such tax year that precede January, 1999. For example, a taxpayer with a tax year beginning October 1, 1998, may deduct 70% of the expense of such meals provided during three months (October 1998 through December 1998).

IV. The taxpayer will not be liable for income tax withholding, FICA taxes, or FUTA taxes on meals provided to taxpayer's employees in the taxpayer's employer-operated, on-premises, eating facility for any tax period ending on or before December 31, 1998.

The settlement initiative is available only to taxpayers in the hospitality industry who have (1) provided free or reduced charge meals to employees on their business premises on a regular basis for more than a mere compensatory purpose, and (2) indicated in writing their interest in accepting the offer no later than 30 days after the draft training materials are finalized. The training materials are expected to be finalized by October 31, 1998.

An eligible taxpayer, whether or not currently under examination or in litigation, indicates in writing its interest in accepting the offer under this settlement initiative by mailing the following information to the Southwest District Office, Employee Meals Settlement Agent:

"Taxpayer's Name____

Taxpayer's Address ____

____

Employer Identification Number _____

On behalf of the above-named taxpayer, I am interested in accepting the settlement offer described in Announcement 98-78, I.R.B. 1998-34 (August 24, 1998), relating to the provision of employee meals in an employer-operated, on-premises eating facility. Please send me the appropriate materials.

By ____ Date ______________________________

Title ______________________________"

Mail the above completed request to the following address no later than 30 days after the finalization of the training materials:

Employee Meals Settlement Agent
Internal Revenue Service
4750 West Oakey Blvd.
Las Vegas, NV 89102

The above completed request can also be faxed to (702) 455-1175. For additional information, contact the Southwest District Office by calling the Employee Meals Settlement Agent at (702) 455-1403.

Upon indication of interest, a taxpayer will receive a letter of instructions regarding how to accept the settlement offer. Each taxpayer who accepts the offer will execute a closing agreement (Form 906) to document the resolution of these issues. Employees of a taxpayer who executes a closing agreement will not be liable for income taxes or FICA taxes on the fair market value of meals received in the taxpayer's employer-operated, on-premises, eating facility for any tax period ending on or before December 31, 1998. No agreements other than that with the taxpayer are necessary in order for the employee of such taxpayer to receive the benefit of the settlement initiative.

Taxpayers, including those currently under examination or in litigation, will not be required to accept the terms of the settlement initiative. If a taxpayer does not believe that the offer is appropriate for its case, the taxpayer may decline to participate in the settlement initiative, and the case will be handled under normal procedures. If participation is declined, the final result in a case could be either more or less favorable than the settlement offer, depending on the merits of the taxpayer's position.

The settlement initiative is also described at the "Tax Professional's Corner" of the IRS Web site at http://www.irs.ustreas.gov.

The principal author of this announcement is Thomas Burger, Director, Office of Employment Tax Administration and Compliance (OETAC). For further information regarding this announcement contact Bob Patrick at (702) 455-1403 (not a toll-free call).

Adjustments Following Sales of Partnership Interests; Change of Public Hearing

Announcement 98–79

AGENCY: Internal Revenue Service, Treasury.

ACTION: Change of time and location of public hearing, and extension of time to request to speak.

SUMMARY: This document changes the time and location of the public hearing and extends the date by which commentators should submit requests to speak on proposed regulations relating to the optional adjustments to the basis of partnership property following certain transfers of partnership interests under section 743, the calculation of gain or loss under section 751(a) following the sale or exchange of a partnership interest, the allocation of basis adjustments among partnership assets under section 755, the allocation of a partner's basis in its partnership interest to properties distributed to the partner by the partnership under section 732(c), and the computation of a partner's proportionate share of the adjusted basis of depreciable property (or depreciable real property) under section 1017 of the Internal Revenue Code. In addition, this document announces that persons wishing to testify who are outside the Washington, DC area will be able to make their presentations from a remote teleconference site in Los Angeles, CA.

DATES: The public hearing is being held on Thursday, September 10, 1998, beginning at 1 p.m. (EDT). Requests to speak and outlines of oral comments must be received by Thursday, August 27, 1998.

ADDRESSES: The public hearing will be held in room 3411, Internal Revenue Building, 1111 Constitution Avenue, NW, Washington, DC. The address of the remote teleconference site is listed below under Supplementary Information.

Requests to speak and outlines of oral comments should be mailed to Room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to CC:DOM:CORP:R (REG–209682–94), Courier's Desk, 1111 Constitution Avenue, NW., Washington, DC. Alternatively, taxpayers may submit comments electronically via the Internet by selecting the "Tax Regs" option on the IRS Home Page, or by submitting comments directly to the IRS Internet site at http://www.irs.ustreas.gov/prod/tax-reg/comments.html.

FOR FURTHER INFORMATION CONTACT: LaNita VanDyke of the Regulations Unit, Assistant Chief Counsel (Corporate), (202) 622-7180 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

A notice of proposed rulemaking and notice of public hearing appearing in the Federal Register on Thursday, January 29, 1998 (63 F.R. 4408 [REG– 209682–94, 1998–17 I.R.B. 20]), announced that a public hearing with respect to proposed regulations relating to adjustments to a partner's basis in its partnership interest and a partnership's basis in its assets would be held on Wednesday, July 8, 1998, beginning at 10 a.m. in the IRS Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington DC and that requests to speak and outlines of oral comments should be received by Wednesday, June 24, 1998.

The date and the time of the public hearing have changed. The room number of the Washington, DC location has changed, and one remote teleconference site has been added.

The hearing will be held in room 3411 of the Internal Revenue Building, 1111 Constitution Avenue, NW, Washington, DC. The remote teleconference site is in room 5003 of the Federal Building, 5th Floor, 300 N. Los Angeles Street, Los Angeles, California.

The public hearing will be begin at 1 p.m. (EDT); attendees will be admitted beyond the lobby of the Internal Revenue Building in Washington, DC after 12:30 p.m. The hearing time at the remote teleconference site in Los Angeles will be concurrent with the hearing in Washington, DC. (10:00 a.m. PDT).

Requests to speak and outlines of oral comments should be received by Thursday, August 27, 1998. All persons who have notified the Service by Thursday, August 27, 1998, of their desire to testify will be given the opportunity to do so. Requests should specify the site from which the speaker wishes to testify; if no specific site is named, the speaker will be scheduled to appear in Washington, DC. Requests to testify in Los Angeles should include a telephone number in case the Service needs to contact the speaker prior to the public hearing.

Due to limited seating capacity at the remote teleconference site, no more than 12 people may be accommodated at any one time in the teleconference room. Seating in the teleconference room will be made available based on the order of presentations. IRS personnel will be available at the remote teleconference site to assist speakers in using the teleconference equipment.

The Service will prepare an agenda showing the scheduling of speakers and will make copies of the agenda available free of charge at the hearing. Testimony will begin with the speakers in Los Angeles, and will conclude with presentations by the speakers in Washington, DC.

Cynthia Grigsby,
Chief, Regulations Unit
Assistant Chief Counsel (Corporate).

(Filed by the Office of the Federal Register on August 4, 1998, 8:45 a.m., and published in the issue of the Federal Register for August 5, 1998, 63 F.R. 41754)

Foundations Status of Certain Organizations

Announcement 98–80

The following organizations have failed to establish or have been unable to maintain their status as public charities or as operating foundations. Accordingly, grantors and contributors may not, after this date, rely on previous rulings or designations in the Cumulative List of Organizations (Publication 78), or on the presumption arising from the filing of notices under section 508(b) of the Code. This listing does *not* indicate that the organizations have lost their status as organizations described in section 501(c)(3), eligible to receive deductible contributions.

Former Public Charities. The following organizations (which have been treated as organizations that are not private foundations described in section 509(a) of the Code) are now classified as private foundations:

573 Warren Street HD FC, Brooklyn, NY
A Woman's Place, Asheville, NC
American Bosnia Relief Association, St. Louis, MO
American Friends of Bnos Yisroel Inc., Philadelphia, PA

Annalori Corporation, Colorado Springs, CO
Arizona Quail Preservation Society, Phoenix, AZ
Arts & Education Foundation of Alabama Inc., Birmingham, AL
Asian Americans of Connecticut Inc., W. Hartford, CT
Association of Research Institutes in Art History, Washington, DC
Bill Cobb Ministries Inc., Bethany, OK
Binghamton Outreach Center Inc., Binghamton, NY
Bond Memorial Trust, Vienna, VA
Boston Emerging Industries Center Inc., Worcester, MA
Bread of Life Christian Mission, Plant City, FL
Carlisle Center for Violence Prevention Inc., Carlisle, MA
Centipede Artists Cooperative, Danbury, CT
Child Placement Professionals Inc., Ada, OH
Child Support Recovery Foundation, Mesa, AZ
Clinton County Sheriffs Reserve, Clinton, IA
Coastal Conservation Foundation, Tucson, AZ
Cobb County District Attorneys Anti-Drug Poster Contest Inc., Marietta, GA
College Community Little League Soccer, Cedar Rapids, IA
Colorado Cuees Scholarship Foundation, Denver, CO
Dominican Family Institute Inc., New York, NY
Dr. Jorge Prieto Community Clinic, Chicago, IL
Ellicott City Kiwanis Foundation Inc., Ellicott City, MD
Extended Health Care Services Inc., Montclair, NJ
Faith With Works In Christ Ministries, Hazel Park, MI
Fathers Against Violence Inc., Carlisle, MA
Federation of Gujarati Associations in North America, Spring Valley, OH
Fit for Success Inc., Cohasset, MA
Fourth Ward Freedmans Town Neighborhood Association, Houston, TX
Freedom Today Not Tommorrow Inc., Olathe, KS
Galion Area Betterment Commission Inc., Galion, OH
Gospel Evangelistic Ministries, St. Joseph, MO
Hands on Memphis Inc., Memphis, TN
Helping Hands of America Association, Winston Salem, NC
Historic Sites & Shipwrecks Restoration & Preservation Society Inc., Fort Lauderdale, FL
Inside Out Productions, Houston, TX
Inspirit Counseling Center, San Anselmo, CA
Institute for Research on Spoken Languages Inc., New York, NY
Islandview Village Community Land Trust, Detroit, MI
Jehova Rapha Ministries, Starr, SC
Knoxville Home Child Care Association, Knoxville, TN
KS Nutritional-Neighborhood Services, Houston, TX
Lets Clean It Up, Tasker Village, PA
M & M Community Development Inc., Columbus, OH
Malemte Football Booster Club, Fairbanks, AK
Mayors Youth Center Inc., Granite City, IL
Missoula Center for Responsible Planning Inc., Missoula, MT
Mobile Elder Care, Mobile, AL
Mother Tierras Inc., Havre de Grace, MD
Naples Pop Warner Football Inc., Naples, FL
New Hampshire Tennis Foundation, Contoocook, NH
New Life Dimensions Ministries, Scottsdale, AZ
Open Door Ministries, Seattle, WA
Pacific Pet Care, Redway, CA
Paducah/McCracken County Small Business Center Inc., Paducah, KY
Parents in Need of Enforced Support, Upper Arlington, OH
Peace Envoy International Inc., Bethesda, MD
Project Life Foundation Inc., Goose Creek, SC
Recovery Television Network Inc., Naples, FL
Residence One Corporation, Tampa, FL
Rosedale Historical Society Inc., Rosedale, MD
Salt Council Inc., Las Vegas, NV
Samoa Felagolagomai Inc., Moreno Valley, CA
Seniors Foundation Inc., Boston, MA
Southwest Louisiana Economic Development Inc., Lake Charles, LA
Southwest Wings Inc., Sierra Vista, AZ
St. Jude Day Care Center Incorporated, Memphis, TN
Tabernacle of Testimony Sanctuary Ministries, Suitland, MD
Tampa Bay Friends for Life Education Fund Inc., Tampa, FL
Tewksbury Girls Softball Inc., Tewksbury, MA
Tiger Haven, Kingston, TN
Toppers Association Inc., Brooklyn, NY
Totus Tuus, Winnetka, IL
United Compassionate Artists Project, Bend, OR

If an organization listed above submits information that warrants the renewal of its classification as a public charity or as a private operating foundation, the Internal Revenue Service will issue a ruling or determination letter with the revised classification as to foundation status. Grantors and contributors may thereafter rely upon such ruling or determination letter as provided in section 1.509(a)–7 of the Income Tax Regulations. It is not the practice of the Service to announce such revised classification of foundation status in the Internal Revenue Bulletin.

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified*, below).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified* and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.

Acq.—Acquiescence.

B—Individual.

BE—Beneficiary.

BK—Bank.

B.T.A.—Board of Tax Appeals.

C.—Individual.

C.B.—Cumulative Bulletin.

CFR—Code of Federal Regulations.

CI—City.

COOP—Cooperative.

Ct.D.—Court Decision.

CY—County.

D—Decedent.

DC—Dummy Corporation.

DE—Donee.

Del. Order—Delegation Order.

DISC—Domestic International Sales Corporation.

DR—Donor.

E—Estate.

EE—Employee.

E.O.—Executive Order.

ER—Employer.

ERISA—Employee Retirement Income Security Act.

EX—Executor.

F—Fiduciary.

FC—Foreign Country.

FICA—Federal Insurance Contribution Act.

FISC—Foreign International Sales Company.

FPH—Foreign Personal Holding Company.

F.R.—Federal Register.

FUTA—Federal Unemployment Tax Act.

FX—Foreign Corporation.

G.C.M.—Chief Counsel's Memorandum.

GE—Grantee.

GP—General Partner.

GR—Grantor.

IC—Insurance Company.

I.R.B.—Internal Revenue Bulletin.

LE—Lessee.

LP—Limited Partner.

LR—Lessor.

M—Minor.

Nonacq.—Nonacquiescence.

O—Organization.

P—Parent Corporation.

PHC—Personal Holding Company.

PO—Possession of the U.S.

PR—Partner.

PRS—Partnership.

PTE—Prohibited Transaction Exemption.

Pub. L.—Public Law.

REIT—Real Estate Investment Trust.

Rev. Proc.—Revenue Procedure.

Rev. Rul.—Revenue Ruling.

S—Subsidiary.

S.P.R.—Statements of Procedral Rules.

Stat.—Statutes at Large.

T—Target Corporation.

T.C.—Tax Court.

T.D.—Treasury Decision.

TFE—Transferee.

TFR—Transferor.

T.I.R.—Technical Information Release.

TP—Taxpayer.

TR—Trust.

TT—Trustee.

U.S.C.—United States Code.

X—Corporation.

Y—Corporation.

Z—Corporation.

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[1] A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 1998–1 through 1998–28 will be found in Internal Revenue Bulletin 1998–29, dated July 20, 1998.

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